THE USAGE OF IFRS IN FINLAND AND GERMANY

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ABSTRACT

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In this thesis paper the author examined how widely spread the use of the International Financial Reporting Standards (IFRS) is among small and medium sized companies in Finland and Germany. Also the reasons behind their decision to adopt or decline the use of the standards were analyzed. The benefits and disadvantages the companies perceived from the standards were also determined.

To achieve this, a quantitative research method was chosen utilizing an online questionnaire, which was sent to companies from all fields of business throughout Finland and Germany. The questionnaire consisted mainly of quantitative questions, but also had open ended questions bringing in a qualitative aspect. This way the companies were able to elaborate on the earlier given answers.

The results were examined regarding the IFRS usage percentage and attempting to understand the reasons behind the companies' decision whether to use or decline the use of the standards. For this the companies were inquired about the benefits and disadvantages of the standards that they have perceived for themselves. The next step was to compare the results of both countries to each other highlighting the differences and similarities.

The analysis indicated the main reasons of German companies to use the standards to be an actual or future listing on the stock exchange or business abroad. The complexity and high expenses of IFRS adoption for small and medium sized companies came out to be the main reasons for not utilizing it.

The Finnish companies appeared to have the same reasons for adopting the new standards as the German companies, but for them the major reason against it were the high costs alone - not the complexity.

These findings can be used for evaluating the benefits and disadvantages, that applying of International Financial Reporting Standards will provide for small and medium sized companies. This information can be valuable for improving the set of standards used for small and medium sized companies. The companies can use the results to evaluate the suitability of the IFRS for their business.

Keywords

IFRS, Accounting, Standards, Germany, Finland, SME

CONTENTS

1 Introduction

1.1 Scope of the thesis

This thesis is done as part of a Bachelor’s degree in International Business. It is not done in commission for a company, but the topic was chosen from the author’s own field of interest.

After reading about the International Financial Reporting Standards, the question occurred how many small and medium sized companies actually voluntarily choose to use the International Financial Reporting Standards (IFRS). This question also led to finding out the reasons behind applying the IFRS or alternatively keeping on using the German or Finnish standards.

A questionnaire based on quantitative research methods with a few qualitative questions was used to find out how far the usage of IFRS is spread and why or why not companies use it.

Using the TAMK forms editor, the questionnaire was created, saved online and sent electronically to companies, who then anonymously answered to it. The answers were received in Excel format, which provides for a favorable environment for analysis.

The answers of the questionnaire will be analyzed considering the country specific accounting practices and regulations, which naturally affect the outcomes of the study. To give the reader an understanding on the accounting practices in the respective countries, they will be explained before the actual examination of the study results.

The presumption regarding the outcomes of the study is that companies will prefer to continue using the national standards instead of adopting the IFRS, as most small and medium sized enterprises (SME) would not have great advantages compared to the disadvantages the new standards would bring.

To reach an understanding on why the respondents chose to use or to decline the use of the IFRS, their answers regarding the benefits and disadvantages of the IFRS will be examined, as those give valuable information on what are the reasons behind their decision.

Finally the outcomes will be analyzed and the results will be compared to point out possible differences between both countries. Analysis will start from the assumption that there is no significant difference between the countries, as in both countries the IFRS is optional for SME and therefore SME has few reasons to choose the new standards over the old ones.

1.2 Structure of the thesis

In the first chapter, the scope of the thesis is presented. The reader gains an understanding of the purpose and main questions of the thesis and is presented with the methods of research used in the process. Also the presumptions the author used before the actual analysis took place are explained in this chapter.

In the second chapter the differences between the two research methods used for a questionnaire will be illustrated. After explaining the differences between quantitative and qualitative research, the choice of methods done for the purpose of this study will be specified and explained.

The third chapter concentrates on the International Financial Reporting Standards and the IFRS Foundation. Here will be explained what the IFRS are and the reasons why they came into being. The structure of the IFRS Foundation will also be analyzed and the specific functions of the different segments will be explained.

The fourth chapter gives an overview of the actual accounting practices in Germany and gives the reader an understanding of the starting conditions, the IFRS were facing when starting to spread their reporting standards in Germany.

In the fifth chapter the accounting practices in Finland are analyzed and like in the earlier chapter, the reader will be given an overview of the local standards that are used as an alternative to the IFRS for small and medium sized companies.

In chapters six and seven the actual analysis of the study results is done. In those chapters the responses received from companies in Germany and Finland will be examined. Here the benefits and disadvantages of the IFRS according to the companies are analyzed. The other factors contributing to deciding for or against the adaptation of IFRS will also be examined.

In the end of both chapters the findings will be summarized and the main reasons for or against the use of the IFRS will be highlighted.

Finally, in chapter eight the results received from both countries will be compared. Here one can see the similarities and differences in both countries. In this chapter also the benefits and the disadvantages the companies perceived from the IFRS usage will be analyzed taking into account the country specific differences.

Chapter nine summarizes the main points of the earlier chapters and gives the reader an overview of the findings done during the analysis. It will highlight the conclusions drawn and summarize the process of getting to those conclusions.

1.3 Research Methods

There are two main approaches to follow when doing a research, quantitative and qualitative research. Those two types of research anyway concentrate on different kinds of questions to be answered. While quantitative research tries to put the phenomenon observed into statistically evaluable terms, qualitative approach tries to find explanations of why two variables affect each other leading to the statistical results found in quantitative research (Carl D. McDaniel, R. Gates, Marketing Research Essentials, 2001).

Quantitative research is used to draw conclusions about how widely spread the researched phenomenon is among the chosen target audience. To ensure that the sample is representative for the population, the sample size is big and respondents are randomly chosen. Another factor a quantitative researcher needs to keep in mind whenever doing a research is the statistical significance.

"How often things occur by the merest chance."
—Terence, Phormio

This quote from the Phormio of Terence (Richard Lowry, 1999-2012) sums the theory behind the term statistical significance surprisingly accurately up. It basically means the chance that the findings of one study are true. Statistical significance anyway is not to be confused with practical significance. A statistical significant result of a survey may or may not be of any practical significance (Professor Kevin McConway, The Open University).

One example would be a survey about customer satisfaction. 2000 customers have been asked how satisfied they are with the local grocery store. The result of the study showed that women were 2% more satisfied with the store than men. The result is statistically significant, but 2% difference does not suggest a big practical significance.

To make the results of the survey statistically measurable, the questions in such surveys tend to be yes/no questions or multiple choice questions. This way the input of respondents is limited to a certain set of answers, which usually does not allow additional explanations to be added. (McLeod, S. A. (2008). Simply Psychology; Qualitative Quantitative.).This way the number of times a certain answer has been chosen can be counted and the conclusions can be drawn about the general opinion or preferences of the target audience.

As Strauss states, qualitative research can be defined as “any type of research that produces findings not arrived at by statistical procedures or other means of quantification”. Statistical research intends to explain phenomena from the subjective viewpoint of the participants. To achieve that, several different approaches are used. The most common methods include observation research, in-depth interviews and focus groups.

In observation research the researcher “monitors respondents’ actions without direct interaction” (Carl D. McDaniel, R. Gates, Marketing Research Essentials, 2001). Observation can take place with different levels of researcher participation reaching from external participation, which “constitutes the lowest degree of involvement in observation” and “can be done by observing situations on television or videotape”(James P. Key, Oklahoma State University) to total participation, in which the researcher is by default also a participant.

In-depth interviews are done between the researcher and participant. Questions of in-depth interviews tend to be open ended, as the objective of the interview is not to get answers to certain questions but to find out the underlying opinions and attitudes of the participants.

In a focus group interview, the researcher steps back from the role of the interviewer and functions more as moderator between the participants. The main goal of a focus group therefore is not to get questions answered by each of the participants but to gain data by encouraging conversation between the participants about a specific topic or area of topics.

For the thesis project a quantitative approach is used. A survey about the application of the IFRS will be sent to companies of all business fields and regions throughout Germany and Finland. The survey anyway will have as a qualitative feature some open ended questions to give the respondents the possibility to give further information about the topic than multiple-choice or yes/no- questions could offer.

2 The International Financial Reporting Standards

2.1 The Standards

The International Financial Reporting Standards (IFRS) are a set of accounting standards developed by the International Accounting Standards Board (IASB) that is becoming the global standard for the preparation of public company financial statements (American Institute of Certified Public Accountants).

Financial reporting is an important source of information to primary users, e.g. investors. Yet there are country-specific differences among the way financial statements are made. The International Accounting Standards Board therefore has developed the IFRS to diminish those differences and harmonize the financial report quality throughout different countries.

The IFRS consists of 9 effective standards, 29 international accounting standards (IAS), 15 Interpretations originated from the International Financial Reporting Interpretations Committee (IFRIC) and 10 SIC (Standing Interpretations Committee) interpretations.

Besides the full IFRS, the IASB has also created an IFRS for SMEs, which is "a self-contained standard of 230 pages, designed to meet the needs and capabilities of small and medium-sized entities (SMEs)" (IFRS Foundation, 2011). In comparison to the full IFRS the complexity had been greatly reduced in several ways. Concerning the differences to the full IFRS, the IFRS Foundation states, that:

- "Topics not relevant for SMEs are omitted. Examples: earnings per share, interim financial reporting, and segment reporting.
- Where full IFRSs allow accounting policy choices, the IFRS for SMEs allows only the easier option. Examples: no option to revalue property, equipment, or intangibles; a cost-depreciation model for investment property unless fair value is readily available without undue cost or effort; no 'corridor approach' for actuarial gains and losses.
- Many principles for recognizing and measuring assets, liabilities, income and expenses in full IFRSs are simplified. For example, amortize goodwill; expense all

borrowing and R&D costs; cost model for associates and jointly-controlled entities; no available-for-sale or held-to-maturity classes of financial assets.

- Significantly fewer disclosures are required (roughly 300 versus 3,000).
- The standard has been written in clear, easily translatable language.
- To further reduce the burden for SMEs, revisions to the IFRS will be limited to once every three years."

The IASB has as well published a Conceptual Framework for Financial Reporting, which handles topics about the preparation of financial reports and their presentation to external users. It is not an IFRS, which means that it does not provide specific standards nor has it priority over any existing IFRS should a conflict between IFRS and Framework arise. Its main purpose is to assist preparers, auditors and standard-setting bodies to comply with the IFRS and to help over possible gaps in the existing set of IFRS (IFRS Foundation).

2.2 The IFRS Foundation

The IFRS Foundation consists of six different parts, namely the IFRS Foundation, the International Accounting Standards Board (IASB), the Monitoring Board, the IFRS Interpretations Committee, the IFRS Advisory Council and working groups formed by the IASB.

The structure of the IFRS Foundation can be seen in Figure 1. In the middle, there is the IFRS Foundation, which consists of 22 trustees of which six must be selected from each Asia/Oceania, Europe and North America, while Africa and South America contribute one member and two are freely selected from the rest of the world. The backgrounds of the IFRS Foundation's members' need to be balanced to ensure the presence of different professional views on the accounting standards. Its functions reach from fundraising and financing for the IFRS Foundation to appointing members to and overseeing the IASB (Deloitte Global Services Limited, 2011).

The IASB is a independent body of the IFRS Foundation responsible for creating the international financial accounting standards as well as those for SMEs and promoting the use of theses standards around the world.It also approves interpretations the IFRS Interpretation Committee provides. The IASB consists at the moment of 15 members which like in the IFRS Foundation are of balanced geographical regions and professional backgrounds.

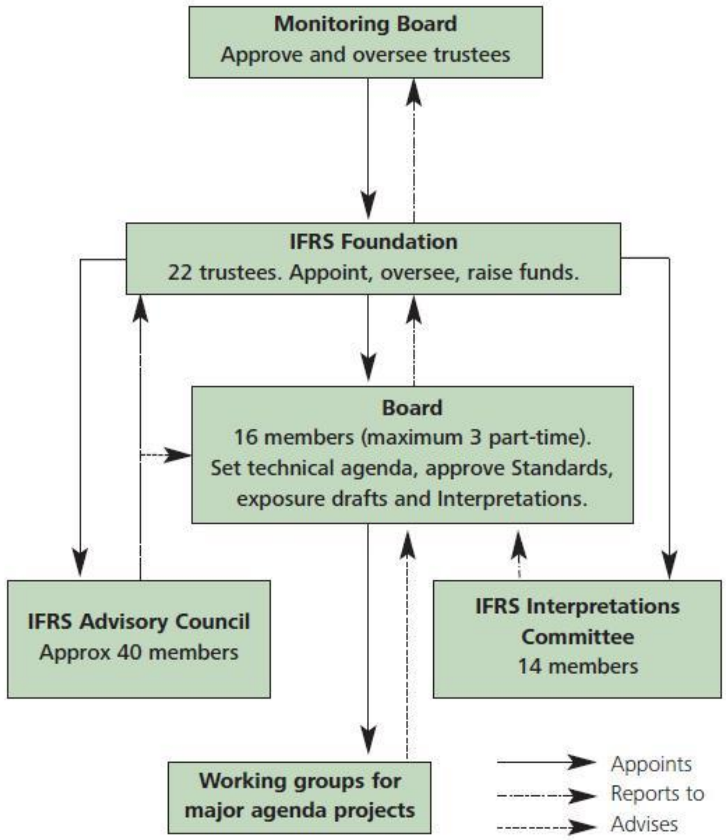


Figure 1: Structure of the IFRS Foundation

The IFRS Interpretations Committee's 14 members are appointed by the IFRS Foundation trustees. Their main responsibility is to "review on a timely basis widespread accounting issues that have arisen within the context of current IFRSs and to provide authoritative guidance (IFRICs) on those issues" (IFRS Foundation, 2011). They as well give consideration to public opinions by publishing draft interpretations to be commented. Finally, as Figure 1 suggests, the members of the Interpretations Committee receive approval of their interpretations and drafts.

The Monitoring Board oversees the trustee selection of the IFRS Foundation and functions as a connecting link between the IASC and the capital market. "The Monitoring Board comprises the relevant leaders of the European Commission, the Japanese Financial

Services Agency, the US Securities and Exchange Commission, the Emerging Markets Committee of IOSCO, and the Technical Committee of IOSCO. The chairman of the Basel Committee on Banking Supervision is a non-voting observer" (Deloitte Global Services Limited, 2011).

The main task of the IFRS Advisory Council is, as the name suggests, advising the IASB on different areas. As the IASB itself, the IFRS Advisory Council consists of members with different geographical and professional backgrounds, but has in comparison to the IASB with actually around 40 trustees significantly more members. The IFRS Advisory Council gives its members a way to actively influence the development of the IFRS, therefore a part of the members are representatives of companies on which the IFRS has effect. As seen in Figure 1, those trustees are appointed from the IFRS Foundation and their set of tasks "includes, but is not limited to, the following:

- input on the IASB's agenda;
- input on the IASB's project timetable (work programme) including project priorities, and consultation on any changes in agenda and priorities; and
- advice on projects, with particular emphasis on practical application and implementation issues, including matters relating to existing standards that may warrant consideration by the International Financial Reporting Interpretations Committee."(SAC, 2004)

Working Groups are formed by the IASB for their major project. They consist of a diverse set of professionals with experience in the specific area at hand, so that the IASB can profit from different viewpoints on the topic in question. The IASB has established working groups for six different projects, being the:

- Employee Benefits Working Group
- Insurance Working Group
- Joint International Group on Financial Statements
- Financial Institution Advisory Group on Financial Statement Presentation
- Financial Instruments Working Group
- Lease Accounting Working Group

Working Groups help the IASB with their expertise to find possible difficulties of their respective projects and to give advice on how to handle them. The IASB may also request advice on implementation issues that may arise as the project proceeds.

3 The German Accounting Practices

3.1 The German Commercial Code

The German Accounting Practices are mainly based on the Handelsgesetzbuch (German Commercial Code) and the Grundsätze ordnungsgemässer Buchführung (German Principles of Proper Accounting).

The actual German Commercial Code has been formed through a series of changes after replacing the Allgemeines Deutsches Handelsgesetzbuch (General German Commercial Code) in 1897, which was the first codified commercial code in Germany and became effective in 1861 after the federal assembly of the German Confederation.

In 1998 the Handelsrechtreformgesetz (HRefG) came into force, which allowed business people a bigger range of possibilities when creating their business. It also regulated the way businesses were classified according to their business operations.

As well in 1998, the Gesetz zur Kontrolle und Transparenz im Unternehmensbereich (KonTraG) was issued. The main purpose of this law was to improve corporate governance and transparency in German companies. The amendments made by the KonTraG to the German commercial code concentrated mainly on the companies' risk management and communication between the company and its owners. The KonTraG is anyway mainly relevant for companies which are listed on a stock exchange or companies with limited liability who have a supervisory board.

The Transparenz- und Publizitätsgesetz (TransPuG) became effective in 2002 and aims at making the German market more attractive for foreign investors by widening the scope of necessary publications the companies need to make, to finally increase the level of transparency in company governance. For example, the TransPuG required from companies to provide a cash flow statement and to perform segment reporting (Prof. Dr. Gerhard Scherrer, 07,2003).

The Bilanzrechtsreformgesetz in 2002 made the IAS mandatory for publicly listed companies, while leaving private companies the choice whether or not to prepare consolidated financial statements in accordance to the IFRS.

The Bilanzrechtsmodernisierungsgesetz (BilMoG) came into effect in 2009 and aimed at providing small and medium-sized enterprises an affordable alternative to the rather extensive IFRS, which would allow them to make high-quality standards (Ernst&Young GmbH, 04.2009). Sole proprietors were completely exempted from the requirement to prepare financial statements, as long their business does not exceed a certain size.

3.2 The German Principles of Proper Accounting

The Principles of Proper Accounting are a set of accounting rules in written or unwritten form. The unwritten rules are derived from common practices and recommendations. They are not codified, but are anyway seen as principles of proper accounting.

The written principles anyway comprise of a set of rules, which are easy to understand and follow. In chronological order those rules are:

> *The accounts must be designed in that way that they give a competent third party within reasonable time an overview of the transactions and the position of the company.* (HGB, § 238)

This means that the accounts need to be complete and the transactions marked in chronological order. Also the accounts themselves need to have a clear structure and need to me marked according to their respective purposes.

> *The records are to be made in a living language. The meaning of abbreviations, numbers, letters or symbols needs to be defined and unchanging throughout the record.* (HGB, § 239)

Basically, this rule states that the records cannot be made in a dead language, e.g. Latin, or in an obsolete dialect. Any kinds of symbols or abbreviations need to be defined and they cannot change their meaning after their initial definition anymore.

> *The entries made into the books are required to be in a complete, correct, timely and orderly manner.* (HGB, § 239)

This rule states that all entries that are made into the books need to be in chronological order and there may not be anything missing from the entry. They need to be done in the same manner as the ones before to avoid misunderstandings. Also e.g. receipts should be filed in timely order and numbered accordingly.

> *Changes must be done in a way that leaves the original entry visible. Furthermore changes may not be of that kind, which leaves uncertainty when the change has been done.* (HGB, § 239)

When changing an entry in the books, one may not simply erase or overwrite the old entry, but must mark the change as such. Also it is required that is it evident when the change has been done, for example by adding a date to the new entry.

> *A copy of all business letters including invoices and payment receipts must be kept in written form for six years after end of the financial year. The copy must equal the original text.* (HGB, § 238)

This in fact means that all business letters concerning a sale or purchase need to be preserved and put in order. The choice about in which way the business letters are organized is done by the accountant, but the letters need to be organized in a consistent way.

> *It must be ensured that the books and documents can be during the storage period made available and readable within reasonable time.* (HGB, § 239)

The required storage period has a minimum of seven years, but should the tax office have a doubt of tax evasion, they may require insight into the books still after ten years.

Germany adopted the IFRS in 2005, which meant that the International Reporting Standards became mandatory for all companies listed on the stock exchange. Anyway, companies which were not listed on the stock exchange may choose whether to adopt the new standards or to continue using the national standards.

4 The Finnish Accounting Practices

There were several key events that affected the Finnish accounting practices. The best way to start the topic is to give an overview of important events in the Finnish history and accounting. In figure 2, there is a list of the key events starting with the conquering of Finland by Tsar Alexander in 1809.

1809 The Russian Tsar Alexander I conquered Finland

1860 Finland got the own money, the Finnish Mark

1862 Lilius' textbook on accounting was published

1917 Finland became an independent country

1918 The civil war

1925 The first Accounting Act

1928 The Publication of Financial Statements Act

1945 Professor Martti Saario outlined the revenue expense theory

1968 The Companies Income Taxation Act was grounded on the Saarios theory

1973 The Accounting Act was grounded on the Saarios theory

1995 Finland joined EU

1997 The Accounting Act was grounded on EU`s 4. and 7. directive

2002 Euro became to the money of Finland

2005 The IAS/IFRS

Figure 2: Key events in Finnish history and accounting

Two years after Finland got an own currency, the Finnish Mark, August Lilius published his book Käytännöllinen opastus Yksinkertaisesta kirjanpidosta varsinkin Tehdastelijoille ja Ammattilaisille (A practical guide to simple bookkeeping especially for Industry and Professionals).

This book was the first accounting textbook in Finnish language. Lilius aimed at giving professionals a guide towards understanding bookkeeping as this was required for all business owners. He defines in his book a form of simple bookkeeping in which there is one account for each creditor or debtor, therefore every transaction with this particular creditor or debtor was entered in the respective account. Besides that "one significant aspect was that Lilius kept the owner and his property not separated from each other; they were the same entity."(Aila Virtanen, The Finnish Accounting History, 02.2004).

In 1925 Finnish government passed the first Accounting Act. This made it obligatory for "everyone required to use a trade name and to register this trade name in the trade register, is as well required to keep books of his or her business' transactions." (Kirjanpitolaki, §1.1, 1925). "The first Accounting Act included simple rules concerning the accounting obligation, the valuation and matching rules, the financial statements and the technique of accounting." (Aila Virtanen, The Finnish Accounting History, 02.2004).

Three years after the first Accounting Act, the Publication of Financial Statements Act was passed in 1928 and it came into force on 1.1.1929. In the new law was required of companies with limited liability to publish their financial statements, specifically the Balance Sheet and the Profit and Loss Statement, within one month after the company's financial statements have been confirmed. (Laki tilinpäätösten julkisuudesta, 118/1928).

In 1945, " Martti Saario invented the expenditure-revenue theory of financial accounting in his doctoral dissertation"(Christopher S. Chapman,Anthony G. Hopwood,Michael D. Shields, Handbook of management accounting research, Nide 2, 02.2007). In his theory, Saario states that the main function of financial accounting is to determine the profits made by the company within a certain period of time.

Therefore the profit-and-loss statement is ranked as the most important, while the balance sheet does not add a lot of value for Saario, as it merely shows the amount of assets and liabilities, but does not help finding the amount of profit made. Saario uses the matching principle in his theory, which means that the total profit or loss made is equal to the total revenue minus the total expenses.

The Companies Income Taxation Act from 1968 took Saario's theory as a foundation. Taxable income according to this Act is all income from business operations in form of cash or other benefits measurable in cash. Tax deductible is all expenses or losses incurred for the purpose of acquiring or retaining profit (Laki elinkeinotulon verottamisesta 24.6.1968/360)

In 1995 Finland joined the European Union, after which the second Accounting Act was passed in 1997, which "is based on the fourth and seventh EC company law Directives, i.e. the so-called Annual Accounts and Group Accounts Directives" (Ministry of Employment and the Economy, 2011).

The fourth directive specifies which financial statements the annual accounts have to contain and how the financial statements have to look like. The European Union provides several layouts and the companies may choose the most suitable for their business. The seventh directive states that a company and its subsidiaries accounts are to be consolidated into group account if the parent company is established as a company with limited liability and it controls or leads its subsidiaries (European Union, 1995-2011).

In 2005 Finland adopted the International Financial Reporting Standards, but so far they have only been mandatory for companies listed on the stock exchange. Small and medium sized enterprises (SME) have so far had the option to either use the IFRS for SME or stay with their old accounting practices.

5 IFRS Usage in Germany

5.1 General analysis

In this chapter, the data received from the online questionnaire will be analyzed and possible conclusions about the usage of IFRS in Germany will be drawn. The online questionnaire was sent to random companies all over Germany and received 20 answers altogether. To begin the analysis, we will have a look at the size of the companies answering the questionnaire.

In Table 1 we can see, that there is a strong tendency in the data received. 55% of all companies answering the questionnaire had between 10 and 50 employees. The other three options were represented equally often, meaning that three companies have fewer than 10 employees, three companies employ between 51 and 250 persons and three answers came from companies with more than 250 employees.

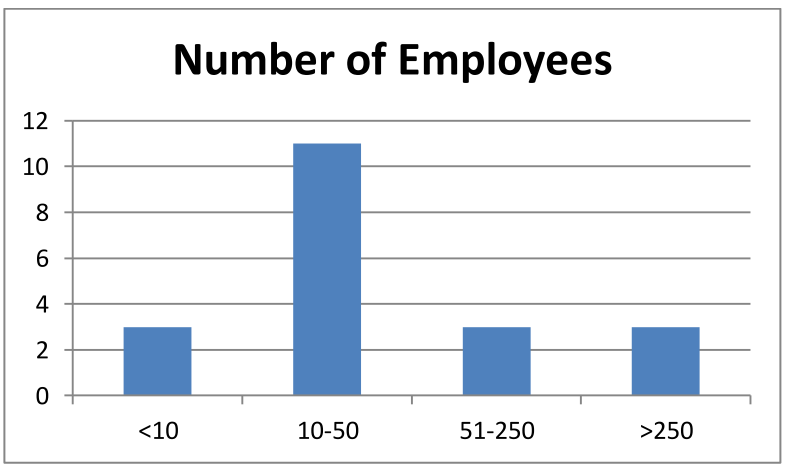


Table 1 Number of Employees

The next thing to examine the number of countries the companies are actually operating in. This question is important as it gives an idea of one possible reason to use the IFRS in case the company is not listed on the stock exchange. Naturally a company which operates in several countries might bear interest in communicating their financial results among the different departments in Germany and abroad. For this the best method would be to have a uniform standard for financial reports, which is used and accepted in all countries in question.

In Table 2 one can see that the main part of companies is operating only in Germany. 50% of all companies stated that their only market is in Germany, but 35% of the answers came from companies operating in two to five countries. The remaining three answers came from companies having business in more than 6 countries, including one stating to have customers in more than 10 countries.

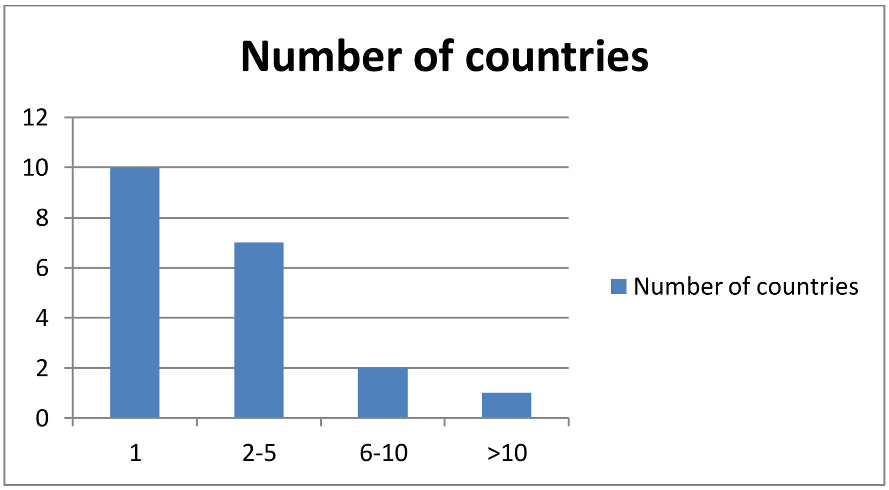


Table 2 Number of countries

The next question on hand would naturally be how these numbers correlate with the usage ratio of IFRS. But to get the correct numbers, one needs to take into account that for companies listed on the stock market it is necessary to use IFRS in their financial reporting, while in the scope of this thesis we are trying to find out how widespread the voluntary adoption of IFRS is and the reasons for that.

One therefore first has to analyze how many companies are listed on the stock market already or how many are planning to get enlisted in the near future and separate them from the rest of the companies using the IFRS.

With sixteen answers, 80% of the respondents are not listed on any stock exchange with no intentions to get enlisted. There anyway are 4 companies of which half are already listed on the Frankfurt stock exchange and the other half are planning to get enlisted in the future.

All of those respondents stating that they are listed or planning to get enlisted on the stock market are currently using the IFRS. For those that are already listed on a stock exchange, it is necessary to use IFRS for their financial reports. When taking a closer look at the answers of those which are planning to get enlisted, it appears that also here the main reason for the usage of IFRS is the future listing on the stock market. The companies find it useful to adopt IFRS early, so when the IFRS becomes necessary for them, they already have experience and are well prepared. They also might have the advantage of being able to fully concentrate on their stock exchange listing, as the IFRS is already well known.

Altogether, there are 8 companies using the IFRS at the moment. As we already found out, 4 of those use the IFRS due to an actual or future enlistment on the stock market, but the next question is why the remaining four are using the IFRS.

To get an answer to this, it is necessary to take a closer look at the companies in question. The companies operate in different fields of business, one being active in the manufacturing business, the other in marketing and the other two in logistics and retail. One interesting detail about all companies in question is that they have interest into taking their business abroad. Three of the four companies operate actually in two to five countries. The remaining company, being active in marketing, is having plans to expand their business to other German speaking countries, like for example Austria and Switzerland.

The business opportunities abroad might be a good reason to use IFRS as, even though not being compelled to publish their financial reports, the companies might want to communicate their financial position to their key customers or alternatively to their divisions abroad. For this a common way of reporting their financial position is necessary, as misunderstandings are inevitable if the parties involved interpret the numbers differently.

Anyway, having business abroad might not be the only reason to voluntarily adopt the IFRS. To find out what other reasons are behind the adoption of the IFRS, the advantages the companies perceive from using the IFRS need to be analyzed.

5.2 The benefits of the IFRS

In Table 3 one can see that 18% of all respondents state that the communication with investors abroad is one of the benefits the IFRS is giving them, which underlines the tendency of companies to use IFRS when having ambitions to operate in more than one country. The benefit of improved communications with investors within the home country was as well stated by 18% of all respondents.

With 12%, the second most chosen option is that applying for funding with a bank is facilitated when using the IFRS in financial reports. The reason for this is that the IFRS demand more detailed and higher quality reports from small and medium sized companies than the German Principles of Proper Accounting and the German Commercial Code demand. This naturally makes it easier for banks to judge the reliability and financial position of the companies applying for funding.

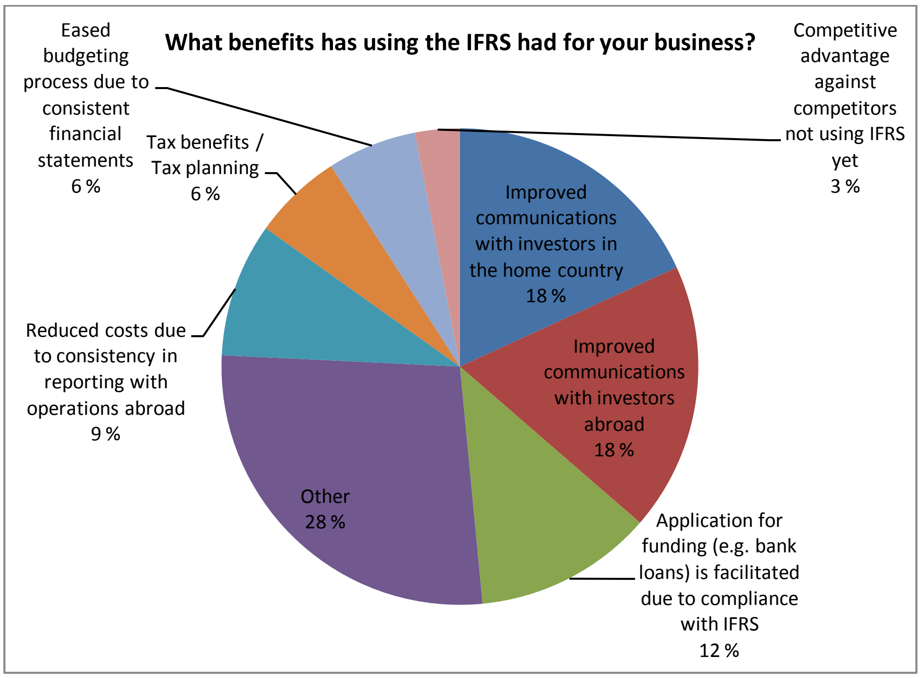


Figure 3 Benefits of IFRS

The third most mentioned advantage is the reduced cost of financial reporting due to consistency with operations abroad. The reason for that may be that when having offices in several countries, it is crucial for the company to know how the financial position of those divisions abroad is. To be able to compare those numbers, the reports need to be prepared after uniform standards, as otherwise the reports would need to be unified later on, creating extra cost for the company.

Other advantages mentioned are tax benefits or tax planning with 6%, eased budgeting due to consistent financial statements as well with 6% and competitive advantage against competitors not using the IFRS yet with 3% of all votes.

After finding out the main reasons for using the IFRS, one would need to analyze as well why the main part of the respondents decided not to use the IFRS in their financial statements.

In the online questionnaire was an open answer field provided for explanations why or why not the companies decided to adopt the IFRS. The answers provided two reasons why the small and medium sized companies choose not to use the IFRS.

The first reason mentioned was that the IFRS is complex and time-consuming, which is a rather big disadvantage for a small company. The second reason found from the open answers was the fact, that the IFRS is not legally necessary for small and medium sized companies with no ambition to get enlisted on the stock market.

Therefore one can expect, considering the fact that the main part of all small and medium sized companies are not using the IFRS in their financial reports, the disadvantages to outweigh the advantages of adopting the IFRS.

Of course, there are as well other reasons behind the choice not to adopt the IFRS. To find out about these, we will take a look at the answers given to the question which were the disadvantages of using the IFRS.

5.3 The disadvantages of the IFRS

In Figure 4, one can see that there were two main concerns. 20% of all companies stated that the cost of preparing financial statements would rise under the IFRS. This underlines the answers the companies have given in the open answer field, as the complex standards require training of the staff and more working time spent on the actual reports.

The second main disadvantage mentioned, as well with 20%, was that older reports need to be revised, meaning an extra amount of work for the company, which naturally also adds to the real cost of adopting the IFRS.

The next most represented option is chosen by 9% of all respondents and states that also the training required for the staff to start using the IFRS is perceived as a disadvantage for the company.

Finally, the last three options, with 6% each, were changes in operations due to adopting the IFRS, the need to update/change computer software and difficulties in adopting the IFRS.

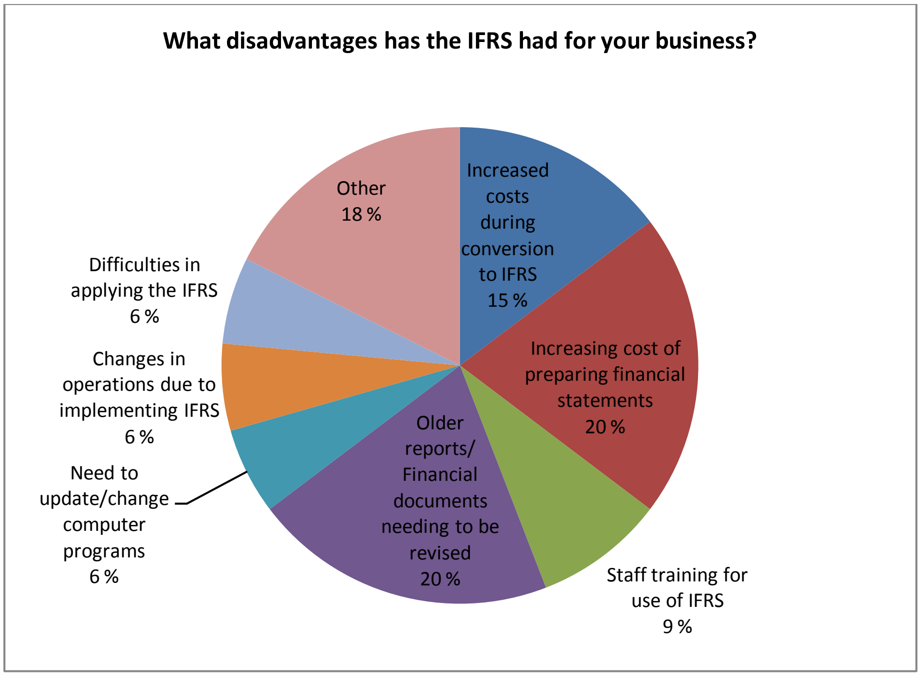


Figure 4 Disadvantages of the IFRS

With an average of 3.3 out of five the difficulty of adopting the IFRS is rated as quite high. The main part of answers to this question came from companies actually using the IFRS in their financial reports. Anyway, three answers came from companies not actively applying the IFRS. Of those, one is stating that the IFRS is too complicated for their use, which is one of the reasons this company is not adopting the IFRS. Another company states that they have outsourced their financial reporting, which means that they do not need to be able to apply the IFRS, but only to analyze reports created using the IFRS.

6.1 Conclusions

Altogether, the reasons for and against using the IFRS have become clear by analyzing the results of the survey. The main two reasons for adopting the IFRS are actual or future enlistment on a stock market and business operations abroad. As the IFRS is not legally necessary for small and medium sized companies, they need to have compelling reasons to adopt the standards. Enlistment on a stock market makes it necessary by law to create the financial reports according to the international standards. As the analysis shows, companies with operations abroad feel that the IFRS gives them an improved way to communicate their financial status with customers or alternatively with divisions in different countries.

The main reasons for companies not using the IFRS are the fact that the standards are very complex and therefore too complicated for small and medium sized companies as well as the costs incurred when adopting the IFRS. For example the cost of educating the personnel for IFRS use or the increased cost of creating financial reports due to the bigger amount of working time used on them.

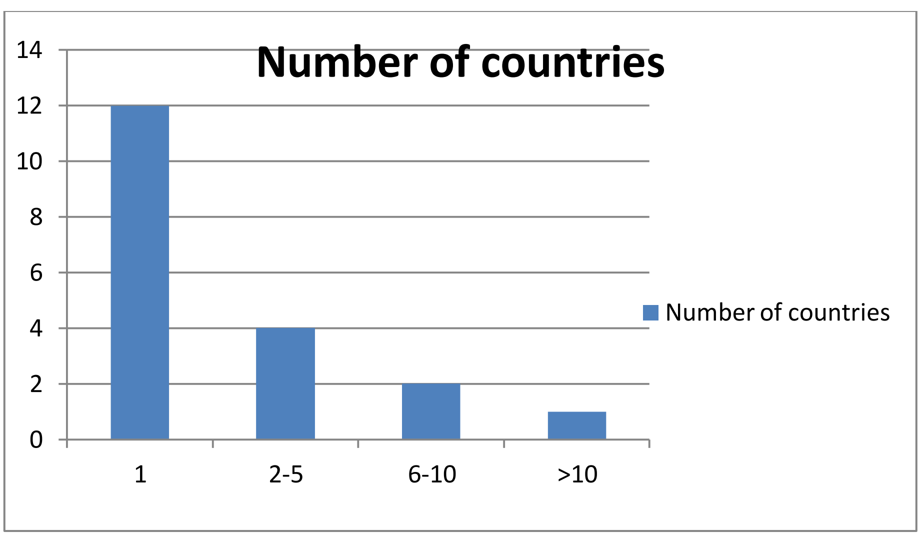
6 The IFRS Usage in Finland

6.1 General analysis

This chapter analyzed the data received from the online questionnaire, which was sent to Finnish companies during the progress of the survey. 19 companies from various fields of business have answered to the questionnaire.

To begin, one should have a look at the size of the companies answering. The majority of the companies, nine companies altogether, employ 10 to 50 employees at the moment. Five companies anyway stated to have less than ten people working for them. There were also five companies with more than 50 employees, of which three stated to have a staff with more than 250 people.

As was found out in the earlier chapter, the amount of countries the companies operate in plays a big role in the decision to use or not use the IFRS. According to the customer data, 63% of all companies are operating only in within Finland. Four companies stated that they have business in two to five countries, making up for 21% of all votes. Lastly, only one company is having operations in more than 10 countries.



Before going to the actual numbers of how many companies are using the IFRS one needs to take a look at how many of the companies are actually listed at a stock exchange. This is, as mentioned in the earlier chapter, important as for listed companies, the use of the IFRS is legally necessary.

According to the survey data, two companies are listed on the stock exchange and another two companies are having plans to get enlisted in the near future. All of these four companies are at the moment using the IFRS for their financial reports. The remaining 78% of all respondents stated that they are not listed on any stock exchange at the moment with no plans to get enlisted in the near future.

The statements in the open answer field pointed out that the companies planning to get enlisted on the stock market found it useful to adopt the IFRS already in advance, since they are obliged by law to do so after the enlistment.

Going further in the analysis process, the next issue to examine is the amount of respondents actually using the IFRS and the reasons for their decision. 42% of all respondents answered in the questionnaire that they are using the IFRS for their financial statements. One interesting fact is that of those eight companies using the IFRS, six are operating in more than one country.

37% of all companies actually using the IFRS are operating in two to five countries, while one quarter states to have business in six to ten countries. Of the remaining respondents 2 have applied the IFRS while having business only in one country at the moment and one has business in more than ten countries.

Anyway, all companies who are either currently enlisted on a stock market or having plans to get enlisted are having business in more than one country. This suggests the conclusion that companies with business abroad are more likely to get enlisted on a stock market, which makes the use of IFRS necessary.

Naturally, this correlation might also come from the fact that companies with customers abroad tend to be relatively bigger compared to those not listed on the stock exchange. Two of the four companies listed on the stock exchange are having over 250 employees at the moment, one is having 51 to 250 employees and the smallest is employing ten to fifty people.

5.2 The benefits of the IFRS

In figure 5, one can see that the main part of the respondents found that IFRS improves their communication with investors or customers abroad. With 13% each, the companies stated that by using the IFRS their communication with investors within Finland improved, they found it easier to gain financial funding from e.g. banks and that using the IFRS gave them a competitive advantage over competitors not using the IFRS yet.

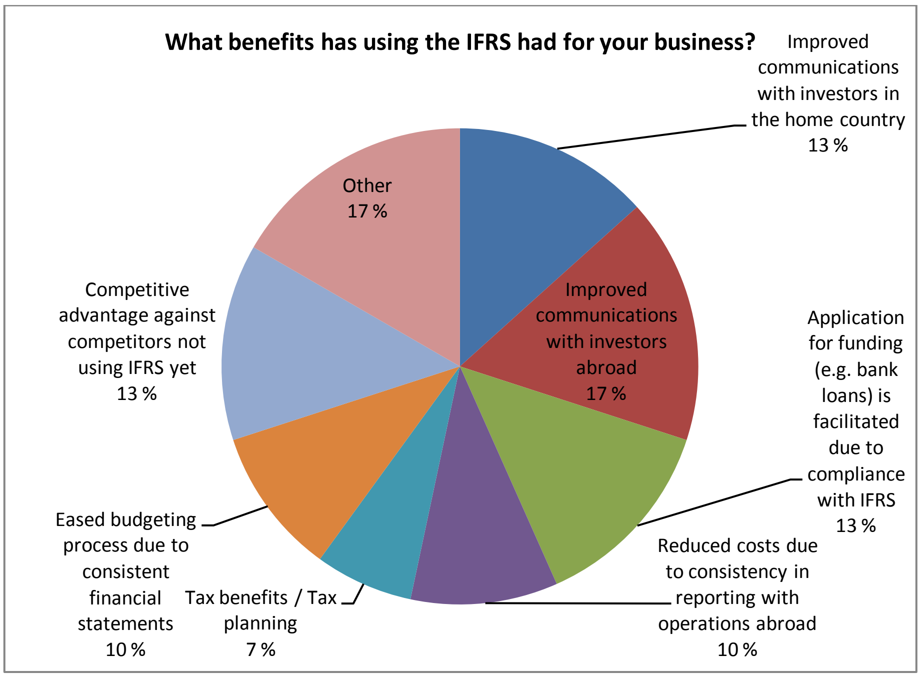


Figure 5 Advantages of the IFRS

Both the advantage of eased budgeting due to consistent financial statements and benefit of reduced costs due to consistency in reporting with operations abroad have been chosen by 10% of all respondents to be an advantage of using the IFRS. 7% stated that using the IFRS eases tax planning and/or gives them an opportunity to gain tax benefits.

Considering that the main part of all respondents stated to have business only in Finland, it is surprising to see that the improved communication with investors abroad was most often mentioned to be an advantage of the IFRS.

One explanation for that would be that companies which are actually having business only within Finland might have plans to expand and therefore find it easier to communicate their financial position to customers or investors abroad. The other explanation naturally is that even though a company has their business only in one country, their end customers might be located around the world, taking as an example an accounting company with offices in Finland and customers throughout Europe.

Using the IFRS appears to provide two advantages for the companies having business within Finland. First, the using the IFRS in their financial reports improves the communication with customers and investors in the home country. The IFRS is setting high standards to quality in financial reports, so it facilitates the reading of the financial statements for customers and investors.

The other advantage the companies in Finland perceived is that using the IFRS facilitates the process of applying for funding, e.g. bank loans. Naturally, a bank will need to check the financial position of an applicant before granting a loan. A high quality financial report done after commonly known and accepted standards gives a clearer picture of the companies’ situation.

5.3 The disadvantages of the IFRS

Next, the disadvantages the companies stated to receive from using the IFRS will be analyzed. The clearly most mentioned disadvantage is the increasing cost of preparing financial statements. This has been chosen by 22% of all respondents. Naturally, as the IFRS is very complex, the preparation of financial statements takes more time and becomes therefore more costly for the companies.

20% of the companies stated that the need of revising older financial documents or reports has for them proven to be a disadvantage of using the IFRS. This underlines the findings that companies feel that the IFRS increases the cost of preparing financial statements.

The working time spent on correcting old reports naturally is an additional cost as also revising old ones is taking valuable time from the employees and slows down the working process, which is further emphasized by the fact that 17% of the responding companies chose that increased cost during conversion to IFRS would be a disadvantage for their company. Seeing the fact that a big part of the respondents state that the IFRS increases the cost of preparing financial statements and that old reports need to be revised, it is not surprising that the conversion can be very costly to companies, especially small and medium sized companies, who do not own a department specially committed to accounting and the IFRS.

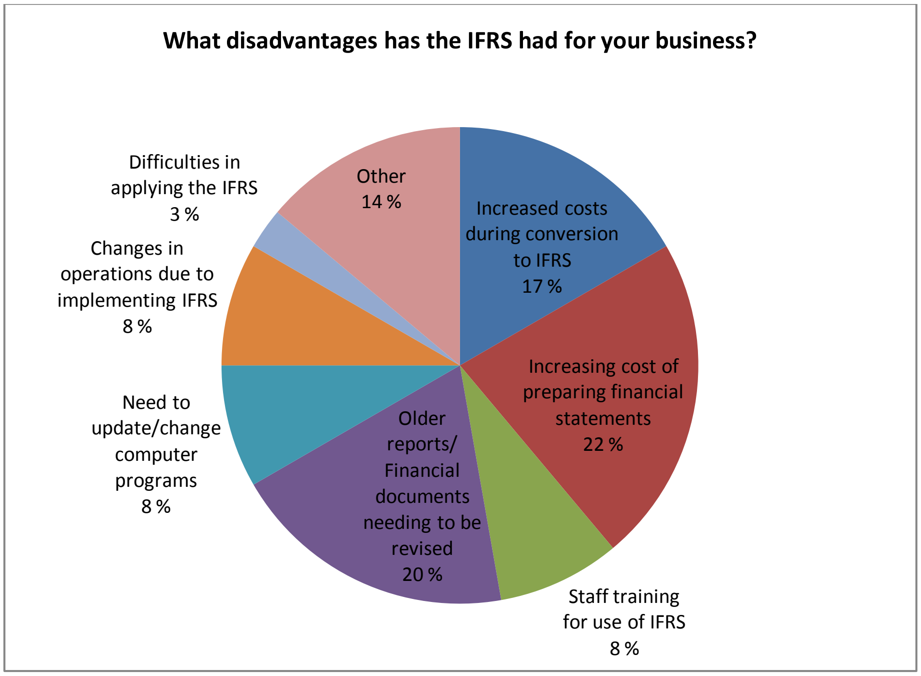


Figure 6 Disadvantages of the IFRS

With 8% each, changes in operations due to implementing the IFRS and the need to update/change computer programs have been chosen to be a disadvantage to the responding companies. For companies, it adds as a cost to change or update computer programs for the use of IFRS.

If the computer program needs to be changed completely, there is on top of the price of the new computer program also the need to train the personnel on the use of the new program. This will slow down the working process at first and in case the training is arranged by a third party, it also brings additional expenses to the company.

5.4 Conclusions

As shown before in the analysis, the two main reasons to use the IFRS are s current listing on the stock market or future plans to do so and business abroad. The listing on the stock market makes the IFRS necessary for companies by law, but when having business in more than one country the companies are having a clear benefit from using the IFRS, as the main part of the respondents stated that the IFRS improves the communication with investors abroad.

The main reason against the use of IFRS is as the companies stated in their responses the high price of converting to the new standards. This increase in price comes from different factors, as they do not only need to train their personnel to apply the IFRS on new standards, but also need to update their existing software or purchase a complete new one. Additionally, older reports and financial statements need to be revised, which as well is taking valuable working time from the employees and adds as a cost to the employer.

8 Comparison between Germany and Finland

In this chapter, the differences and similarities between Germany and Finland regarding the use of the IFRS will be analyzed. Also the reasons for those differences and similarities will be evaluated.

To begin, the most important point to compare will be evaluated being the question how widespread the use of the IFRS is in both countries. The usage percentage of IFRS in Germany was with 42% slightly higher than in Finland with 40%. As shown in the chapters before, the main reasons in both countries were a current or future listing on the stock market and business abroad.

Regarding the amount of companies listed on the stock exchange, the respondents from Finland and Germany are very similar. In both countries, there appear to be two companies which actually are listed on the stock exchange and two with plans for future listings.

When comparing the size of the companies responding to the questionnaire, one can clearly see that the companies in Germany were relatively bigger than the ones in Finland. In the same way that also the size of the companies differ, also the amount of countries they have business in differs. While in Finland 63% of all respondents were having business activities in only one country, in Germany only 50% were confined their home country only.

Considering that the percentage of IFRS usage was with 40% in Finland and 42% in Germany quite equal, it does not surprise to see that both countries are also similar in those factors mentioned to be the main reason for using the IFRS.

The next thing one has to analyze to fully understand the differences and similarities between the two countries is the respective reasons for and against the use of IFRS. For this, one has to look at the responses given about the advantages and disadvantages of the IFRS that the companies have perceived.

8.1 The Advantages of the IFRS

In Figure 7 the comparison between the perceived benefits of respondents from Finland and in Germany are shown. As one can see, the companies in both countries perceive similar things to be an advantage from using the IFRS.

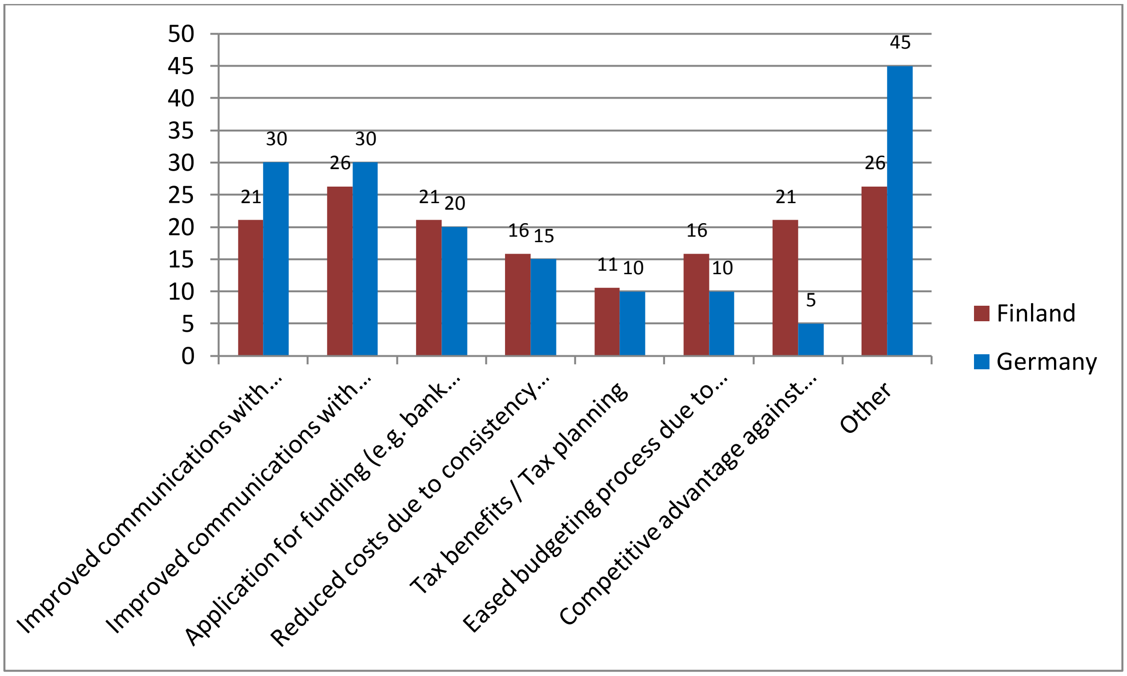


Figure 7 Benefits of the IFRS in Finland and Germany

It anyway is interesting that companies in Germany have more often mentioned that the improved communication with investors in the home country is an advantage of the IFRS, as the responses from Finnish companies showed that in Finland, there are remarkably more companies with customers only in one country.

A possible explanation for that is that for German customers, the use of IFRS has more significantly improved the communication within the home country, as the IFRS is more widely used in Germany than it is in Finland.

Also when it comes to the benefit of improved communications with investors abroad, German companies have stated this to be an advantage for them more frequently than Finnish companies did, even though the difference here is not quite as notable.

This is not an unexpected outcome as German companies, as stated above, tend to have business in more countries than Finnish ones and therefore might perceive the advantage of improved communications outside their home country as a more relevant benefit of the IFRS.

Another notable difference between the answers of both countries is that Finnish companies more frequently mentioned eased budgeting due to consistent financial statements to be a benefit for their business. As the IFRS strongly regulates the content and appearance of the financial reports, companies may benefit from using it, as it makes the tendencies between several financial periods better visible when analyzing the financial statements.

Concerning the statement that IFRS provides a competitive advantage against competitors not using the IFRS yet, the answers from German and Finnish companies differ notably. While 31% of all respondents in Finland stated that they gain competitive advantage by using the IFRS, only 5% of the German companies thought so.

An explanation for this is that, as stated before, the usage of IFRS is not as widely spread in Finland as it is in Germany. It therefore is likely to make those companies using the IFRS in Finland stand out from the mass of companies not using the IFRS, especially to foreign customers and investors.

8.2 The Disadvantages of the IFRS

Further, the disadvantages from using the IFRS will be analyzed. In figure 8, one can compare the answers from both German and Finnish companies regarding the drawbacks of the IFRS for their business.

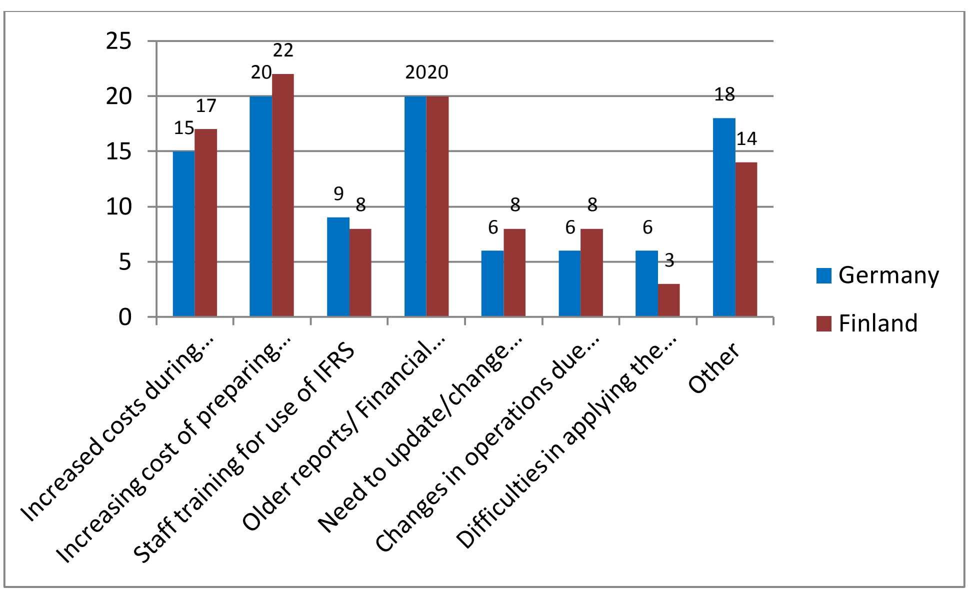


Figure 8 The disadvatanges of the IFRS

Regarding the disadvantages of the IFRS, the answers from German and Finnish companies are very similar. There are anyway small differences in how many companies perceived the increased costs during conversion to the IFRS as a disadvantage of the IFRS. In Finland 17% of all respondents thought that this was a disadvantage for their business, while in Germany only 15% of the companies perceived this a relevantly negative.

One explanation for this is that in Finland, where fewer companies are actually using the IFRS, the costs of adopting it are relatively higher in comparison to the costs incurred by companies in Germany, as they lead to a higher competitive disadvantage in Finland, as other companies do not incur those additional costs.

Another explanation is that due to the lower amount of companies actually using the IFRS in Finland, the relative usefulness in comparison to the price is lower for Finnish companies than for German companies. This basically means that for a Finnish company the IFRS is more expensive in comparison to the advantages it had by applying the IFRs in their financial statements.

The same reasons may also apply to the fact that companies in Finland mentioned the increasing costs of preparing financial statements more often as a disadvantage than German companies.

As one can see in the figure 8, the difficulties in applying the IFRS were felt by notably more companies in Germany as a disadvantage than by companies in Finland. In comparison, 6% of all German companies stated that this is a downside of the IFRS, while only 3% of all Finnish respondents thought so.

This is a surprising fact as in Germany more companies use the IFRS than in Finland, so it would be expected that the information and training opportunities would be better in Germany than in Finland. Anyway, in Germany companies have the tendency to be bigger and have business in more countries, which might complicate the process of adapting the IFRS.

9 Conclusions

The main purpose of the thesis was to find out how many small and medium sized companies in Finland and Germany are actually using the IFRS in their financial statements and the reasons for their decision. This is a relevant question regarding the fact that the IFRS is not legally necessary for companies in both countries, unless they have a listing on a stock market.

For the thesis project a quantitative approach with qualitative features is used. A survey about the application of the IFRS will be sent to companies of all business fields and regions throughout Germany and Finland. The survey itself comprises mainly of quantitative questions, but also has open ended questions, which give the respondents the possibility to elaborate their earlier answers.

Financial reporting is an important source of information to primary users, e.g. investors. Yet there are country-specific differences among the way financial statements are made. The International Accounting Standards Board therefore has developed the IFRS to diminish those differences and harmonize the financial report quality throughout the different countries.

The IFRS Foundation consists of six different parts, namely the IFRS Foundation, the International Accounting Standards Board (IASB), the Monitoring Board, the IFRS Interpretations Committee, the IFRS Advisory Council and working groups formed by the IASB. All the six parts perform different functions reaching from forming new reporting standards or making amendments to older ones to examining evaluating feedback gained from the public.

The German Accounting Practices are mainly based on the Handelsgesetzbuch (German Commercial Code) and the Grundsätze ordnungsgemässer Buchführung (German Principles of Proper Accounting).The German commercial code replaced the Allgemeines Deutsches Handelsgesetzbuch (General German Commercial Code) in 1897 and has gone through series of changes since. The Principles of Proper Accounting are a set of accounting rules in written or unwritten form. The unwritten rules are derived from common practices and recommendations. They are not codified, but are anyway seen as principles of proper accounting.

There were several key events that affected the Finnish accounting practices. The main ones were the publishing of Lilius' book being the first accounting textbook in Finnish language, the passing of the First accounting Act in 1925 followed by the Publication of Financial Statements Act in 1928 and in 1945, "Martti Saario invented the expenditure-revenue theory of financial accounting in his doctoral dissertation"(Christopher S. Chapman,Anthony G. Hopwood,Michael D. Shields, Handbook of management accounting research, Nide 2, 02.2007). In 2005, Finland adopted the International Financial Reporting Standards, but so far they have only been mandatory for companies listed on the stock exchange.

The two main reasons for German companies to use the IFRS are s current listing on the stock market or future plans to do so and business abroad. The main reasons for companies not using the IFRS are the fact that the standards are very complex and therefore too complicated for small and medium sized companies as well as the costs incurred when adopting the IFRS.

The two main reasons for Finnish companies to use the IFRS are s current listing on the stock market or future plans to do so and business abroad. The main reason against the use of IFRS is as the companies stated in their responses the high price of converting to the new standards.

In the comparison of the responses the companies from both countries gave to the questionnaire, one could see that the countries are very similar regarding the use of the IFRS and the companies' perception of the benefits and disadvantages.

The usage percentage of IFRS in Germany was with 42% slightly higher than in Finland with 40%, while the companies in Germany were relatively bigger than the Finnish ones. When examining the answers received from both countries, it became apparent that the companies in both countries perceive similar things to be an advantage from using the IFRS. Also the disadvantages mentioned by the companies were similar with anyway some differences in the frequencies the different options were voted for.

The assumption the author made before the actual analysis was proven to be correct during the examination of the study results. The answers received from the two countries showed that the use of the IFRS is comparably wide spread and the reasons for and against the usage of the new standards are alike in both Germany and Finland.

To improve the usage percentage of the IFRS among small and medium sized companies, the standards need to be adjusted better to the needs those companies have. At the moment the standards are too complex and costly for SME, which shows that they are still too close to the full IFRS.

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