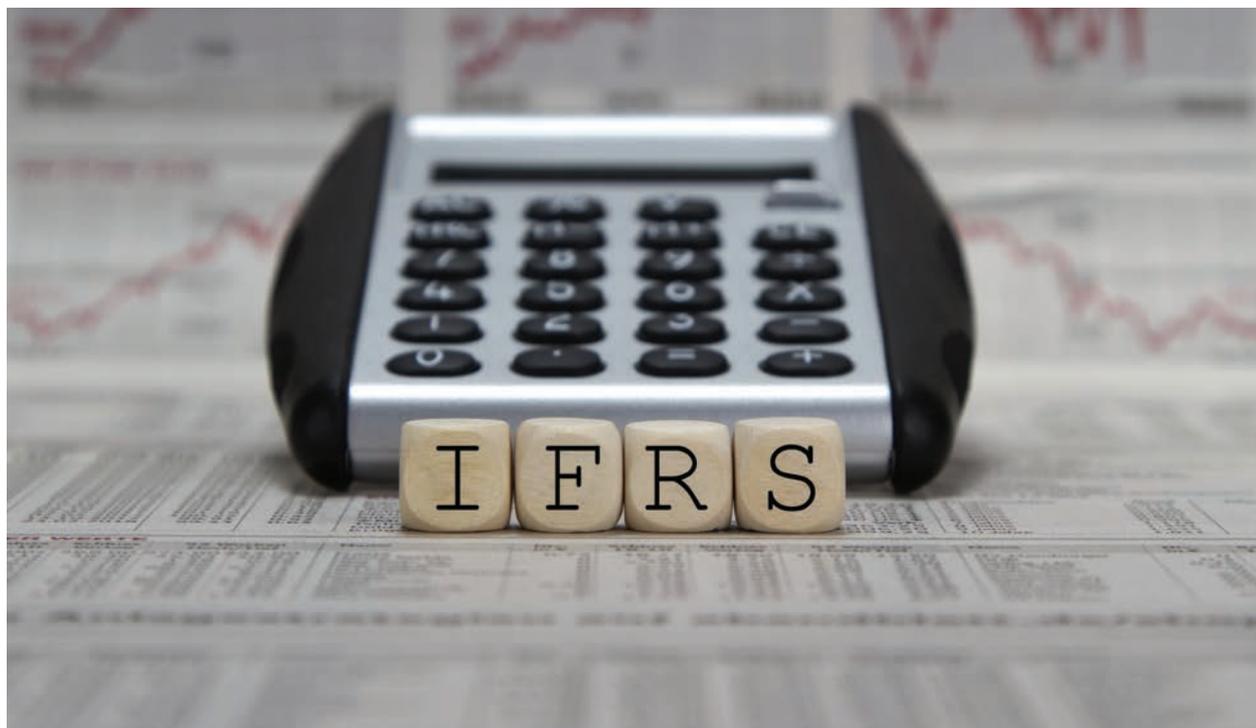


## Consistent Application of IFRS in Asia-Oceania Region: Obstacles and Role of AOSSG<sup>1</sup>



*The accounting literature identifies that accounting practice of a country is greatly affected by the country's culture, legal and regulatory environment or social factors such as language and religion, as well as the level of economic development. To address such issues and to overcome the resulting challenges, the IFRS Foundation utilises the regional bodies like AOSSG to explore IFRS implementation issues and support consistent application. The AOSSG, which aims to provide its culturally and legally diverse region's collective views to the IASB to reflect them in the setting and amending processes of IFRS, promotes the consistent application of IFRS across the region. In this article, the author investigates the potential obstacles to achieving consistent IFRS application in the Asia-Oceania region and explores the possible roles that the AOSSG may play in effectively promoting consistent application of IFRS across AOSSG member jurisdictions. Read on...*



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### Introduction

According to the IFRS Foundation's jurisdictional profiles<sup>2</sup>, 119 of the 143 countries (92%) require IFRS for all or most domestic publicly accountable entities in their capital market (as of March 2016). Considering that the primary goal of IFRS is to provide a single set of high-quality accounting standards that is expected to bring transparency, accountability and efficiency to financial markets

<sup>1</sup> The views and opinions expressed in this article are the author's own and do not necessarily reflect the views of the AOSSG or the KASB.

<sup>2</sup> <http://www.ifrs.org/Use-around-the-world/Pages/Jurisdiction-profiles.aspx>

around the world<sup>3</sup>, the rapid spread of IFRS around the globe in recent years is considered as a remarkable achievement in this respect.

Spreading IFRS as a single set of global accounting standards around the world, however, is only a necessary condition to enhance global financial reporting comparability, not a sufficient condition fundamentally. To improve the quality and comparability of global financial reporting under IFRS, consistent application of IFRS across jurisdictions must be guaranteed.

The accounting literature identifies that accounting practice of a country is greatly affected by the country's culture, legal and regulatory environment or social factors such as language and religion, as well as the level of economic development (Gray 1988; Brown et al 2014). In particular, since IFRS is principle-based accounting standards, it is inevitable to use professional judgment, which would be considerably influenced by social and cultural factors of the country, in applying IFRS. Also, for those jurisdictions whose official language is not English, there always exists a risk of mistranslating or misinterpreting the standards during the translation process. Such factors may function as obstacles to achieving consistent application of IFRS across adopters of IFRS, thereby deteriorating the global financial reporting comparability between countries and/or entities in the long run.

In an endeavor to facilitate consistent application of IFRS and successful implementation of new standards across jurisdictions, the IFRS Foundation operates Transition Resource Groups and the Interpretations Committee, and also made the Post-Implementation Review mandatory. However, there are limits to such efforts in sufficiently resolving practical implementation issues since

the issues usually arise from applying IFRS in widely ranging cultural and social environment. To overcome the challenge, the Foundation now utilises regional bodies<sup>4</sup> like the AOSSG to explore IFRS implementation issues and support consistent application.

The AOSSG is a regional body established in 2009. As many as 26 jurisdictions in the Asia-Oceania region are members of the AOSSG as of now. The objectives of the AOSSG include providing the region's collective views to the IASB to reflect them in the setting and amending processes of IFRS and supporting IFRS adoption in the region. Furthermore, it promotes consistent application of IFRS across the region by identifying common accounting issues in implementation and informing the IASB or Interpretations Committee of the issues to seek solutions.

The AOSSG has a relatively diverse group of member jurisdictions, with differing cultural, legal and regulatory environments and wide disparities in the levels of social and economic development. So it would be fair to say that there exist a significant number of potential obstacles to consistent IFRS application in this region.

### Key Obstacles

Diversity in local GAAP and accounting conventions across jurisdictions is generally explained by vast differences in their culture, legal and regulatory environment, language, enforcement, level of economic development, etc. These factors may be the very factors which cause inconsistencies in IFRS application process in different jurisdictions. Thus, it is highly likely that professional judgments on accounting choices can be influenced by cultural, social and economic factors of each jurisdiction under IFRS, which is considered as principle-based accounting standards.

Literature reports that the primary factors which may affect accounting environment of each country are culture, language, legal origins, legal enforcement, audit power, and economic development as presented in Figure 1. This article focuses on the Asia-Oceania region, in particular, AOSSG member jurisdictions to discuss potential obstacles that hinder consistent application of IFRS in the region. In the light of the discussion, I would like to explore the implications

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<sup>3</sup> Mr. Hoogervorst acknowledged: "Our mission is to develop IFRS that brings transparency, accountability and efficiency to financial markets around the world. Our work serves the public interest by fostering trust, growth and long-term financial stability within the global economy." (16 April 2015)

<sup>4</sup> The regional groups include: (a) Asian-Oceania Standard-Setters Group (AOSSG); (b) European Financial Reporting Advisory Group (EFRAG); (c) Group of Latin-American Standard-Setters (GLASS); and (d) South African Financial Reporting Standards Council, supported by the Pan African Federation of Accountants (PAFA) in alphabetical order.

# Special Write-Ups

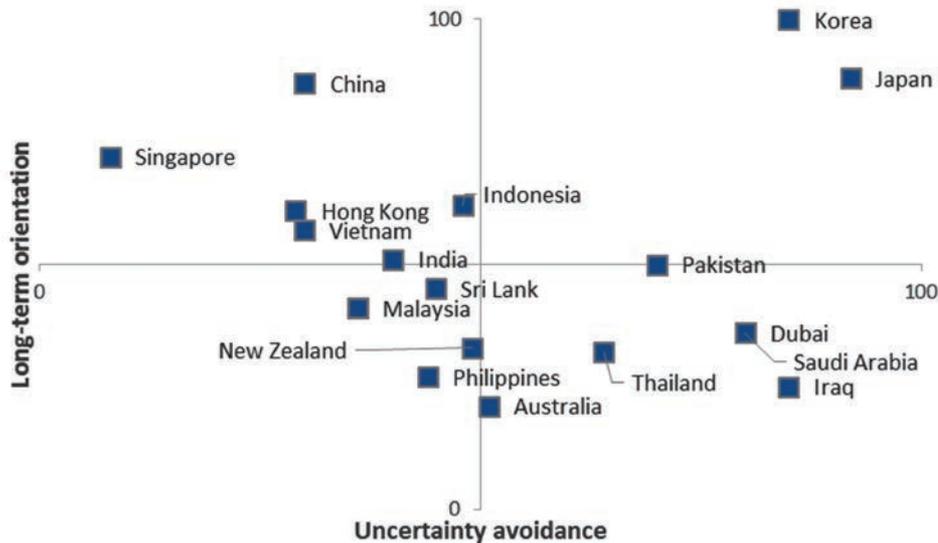
**Gray (1988) developed a theoretical framework of the influence of culture on accounting, based on the cultural dimensions by Hofstede (1980). He showed that conservatism – understatement of gains and assets and overstatement of losses and liabilities in financial statements– is closely related to a high level of uncertainty avoidance and long-term orientation.**

of the AOSSG's role in enhancing consistent IFRS application across the Asian-Oceania region.

Figure 1. Key Obstacles



Figure 2. Conservatism of AOSSG Countries



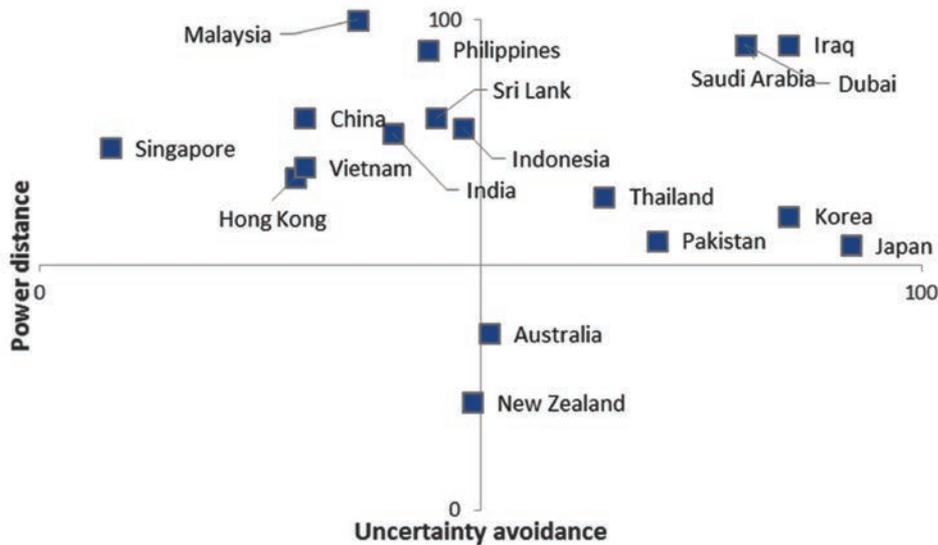
<sup>5</sup> <https://www.geert-hofstede.com/>

## Culture

Culture influences every single aspect of a society, and accounting is no exception. Gray (1988) developed a theoretical framework of the influence of culture on accounting, based on the cultural dimensions by Hofstede (1980)<sup>5</sup>. He showed that conservatism–understatement of gains and assets and overstatement of losses and liabilities in financial statements– is closely related to a high level of uncertainty avoidance and long-term orientation. Also, secrecy–a preference for restriction of disclosure of accounting information–increases as uncertainty avoidance and power distance increase. These findings suggest that the culture of a country is closely linked with the country's accounting values and thus becomes a critical factor that affects the accounting practice in that country.

Figure 2 and Figure 3, respectively, show the level of conservatism and secrecy of AOSSG member jurisdictions. As you can notice from the figures, the level of conservatism and secrecy varies widely from one jurisdiction to another. For example, Korea and Japan seem to be more conservative, while Australia and New Zealand are classified as countries with weak conservatism in Figure 2. Also, Saudi Arabia and Korea show a stronger level of secrecy, whereas Australia, New Zealand and Hong Kong display a lower level of secrecy. These diversities in conservatism and secrecy levels may affect measurement and disclosure of accounting information in accounting practice across jurisdictions, indicating that different cultures may act as potential barriers to consistent application of IFRS.

Figure 3. Secrecy of AOSSG Countries



The Korean Accounting Standards Board (KASB) and the Australian Accounting Standards Board (AASB) have been conducting a joint research project on interpretation of terms of likelihood in IFRS with accounting professionals in Korea and Australia<sup>6</sup>. Results show that a majority of the terms tend to be interpreted inconsistently between the two countries. This, I believe, clearly indicates that different cultures may lead to different interpretations and judgments when applying the same accounting standard, thereby causing the same accounting event to be reflected differently in the financial statements.

Because the cultural factor exists as an inherent factor in the application of accounting standards as explained above, we should be mindful of the cultural gaps between jurisdictions in order to promote consistent application of IFRS.

### Legal Origins

Legal origins play an important role in the development of corporate ownership, corporate

**Also, common law countries are likely to exhibit greater investor protection than code law countries. In terms of accounting standards, local GAAPs of code law countries are more distant from IFRS than those of common law countries. Moreover, other regulatory environment such as tax reporting requirements may vary according to the legal origin.**

capital structure, and capital markets, and affect financial disclosures substantially. For example, firms in code law countries mainly depend on financing from the government, bank or private parties, thus accounting information obtained through private channels is more important than published financial statements. On the other hand, firms in common law countries typically rely on public financing, thus public information provided from financial statements is more important.

Prior studies on legal origins and accounting found some interesting points as follows. Firms in common law countries tend to have higher financial disclosures than those in code law countries, which means that legal origins may affect comparability of financial statements. Also, common law countries are likely to exhibit greater investor protection than code law countries. In terms of accounting standards, local GAAPs of code law countries are more distant from IFRS than those of common law countries. Moreover, other regulatory environment such as tax reporting requirements may vary according to the legal origin. These findings suggest that the legal origins of the jurisdictions that adopt IFRS should also be considered as a factor that hinders consistent application of IFRS across jurisdictions.

Legal origins of AOSSG member jurisdictions classified by La Porta et al. (2008) are presented in

<sup>6</sup> <http://www.ifrs.org/Meetings/MeetingDocs/ASAF/2015/December/1512-ASAF-01-AASB-KASB-Research-Project.pdf>

# Special Write-Ups

Table 1 below that shows diverse legal origins across jurisdictions in the region:

**Table 1. Legal Origins by Members of AOSSG (La Porta et al., 2008)**

English Common Law	French Code Law	German Code Law
Australia	Cambodia	China
Hong Kong	Indonesia	Japan
India	Iraq	Korea
Malaysia	Kazakhstan	Mongolia
Nepal	Macao	
New Zealand	Philippines	
Pakistan	Syria	
Saudi Arabia	Uzbekistan	
Singapore	Vietnam	
Sri Lanka		
Thailand		

## Language

IFRS is originally written in English, and official translations into a number of other languages are provided by the IFRS Foundation<sup>7</sup>. IFRS Foundation notes that translation is a vital part of developing a single set of high-quality global accounting standards for use around the globe. Moreover, translation is often an important factor in a country's decision to adopt IFRS. In the process of translation, there always exist potential pitfalls of mistranslation and even the translated IFRS can be misinterpreted. In some cases, it may be difficult to find equivalent expressions in the target language. Such translation issues may be a potential obstacle to consistent application of IFRS around the world. Furthermore, even if equivalent translations are available, it may not be easy to deliver the exact intended meaning of the concepts if the relevant issues are rarely likely to arise in the accounting culture of a specific country.

**Table 2. Official Languages of AOSSG Member Countries (As of December 2014)**

Country	Language(s)	IFRS Translations
Australia	English (de facto)	No
Brunei	Malay, English	No
Cambodia	Khmer	Yes
China	Mandarin	Yes
Dubai	Arabic	Yes
Hong Kong	Cantonese(de facto), English	No
India	Hindi, English, 21 other officially	No
Indonesia	Indonesian	No
Iraq	Arabic	Yes
Japan	Japanese (national)	Yes
Kazakhstan	Kazakh (national)	n/a
Korea	Korean	Yes
Macao	Cantonese(de facto), Chinese(Traditional), Portuguese	No
Malaysia	Malaysian(national), English	No
Mongolia	Mongolian	Yes
Nepal	Nepali	No
New Zealand	English (de facto)	No
Pakistan	Urdu(national, official), English(official)	No
Philippines	Filipino, English	No
Saudi Arabia	Arabic	Yes
Singapore	English, Chinese, Malay(national), Tamil	No
Sri Lanka	Sinhala, Tamil	Yes
Syria	Arabic	Yes
Thailand	Thai	Yes
Uzbekistan	Uzbek (national)	Yes
Vietnam	Vietnamese	Yes

(Reference: Wikipedia, IASB Jurisdiction profiles)

<sup>7</sup> Official IFRS translations are available in 12 languages on the IFRS Foundation website: Albanian, Arabic, Armenian, Brazilian Portuguese, French, Kazakh, Russian, Spanish, Traditional Chinese, Turkmen, Ukrainian and Uzbek.

As presented in Table 2, there is a wide variety of official languages of AOSSG member jurisdictions. English-speaking jurisdictions are 9 countries which include Australia, Brunei, Hong Kong, India, etc., and the rest of the jurisdictions are classified as non-English-speaking jurisdictions. According to jurisdiction profiles provided by the IFRS Foundation, 13 countries require a translation process in adopting and applying IFRS. Although they are all subject to a translation process, the degree of difficulties and type of issues experienced by each jurisdiction would vary greatly depending on how similar its official language is to English<sup>8</sup>.

### Legal Enforcement

Many jurisdictions have adopted or are considering adopting IFRS to enhance the financial reporting quality and comparability of financial statements across jurisdictions. To achieve this goal, legal enforcement plays a pivotal role in promoting consistent IFRS application. Brown et al. (2014) developed an index which estimates differences in legal enforcement among countries in regard to the institutional setting for financial reporting. They argued that the effect of IFRS adoption may vary depending on the level of legal enforcement of each country, suggesting that discretionary accounting treatment by managers could be more restricted in a country with strong legal enforcement and thus producing higher quality accounting information.

Table 3 presents the level of legal enforcement of some AOSSG member jurisdictions estimated by Brown et al. (2014)<sup>9</sup>. There exist considerable differences in the extent of legal enforcement in each

country. For example, countries such as Australia and Hong Kong display relatively strong legal enforcement, while countries such as Indonesia and Pakistan show relatively low legal enforcement. In order to achieve consistency in the application of IFRS, which in turn improves comparability of financial statements information, legal enforcement should be considered as an important factor.

**Table 3. Legal Enforcement (Brown et al., 2014)**

Country	2002-2004	2005-2007	2008-2011
Australia	38	52	52
China	28	37	37
Hong Kong	24	30	52
India	15	17	21
Indonesia	12	14	14
Japan	16	34	34
Korea	12	24	28
Malaysia	15	17	40
New Zealand	16	39	43
Pakistan	15	18	18
Philippines	6	24	27
Singapore	21	32	32
Thailand	24	26	23

### Audit Power

Differences in audit power across jurisdictions also affect consistency in the application of IFRS. The quality of financial statements is highly related to the quality of audit even though the financial statements are prepared under a single set of standards, such as IFRS. Francis et al. (1999) argue that higher audit quality can reduce bias or errors in financial statements reporting, further improve information environment of firms, and eventually facilitate the production of high quality accounting information. Thus, audit power is also a factor to be considered in consistent application of IFRS across jurisdictions.

Brown et al. (2014) created an audit power index by audit fee, audit rotation, and litigation risk. Table 4 shows considerable variations of audit power indexes of some AOSSG member jurisdictions. Similar to the level of legal enforcement, the audit power index of countries such as Australia and Hong Kong appear to be high, while countries such as Indonesia, Pakistan show relatively low audit power indexes.

**Moreover, translation is often an important factor in a country's decision to adopt IFRS. In the process of translation, there always exist potential pitfalls of mistranslation and even the translated IFRS can be misinterpreted. In some cases, it may be difficult to find equivalent expressions in the target language. Such translation issues may be a potential obstacle to consistent application of IFRS around the world.**

<sup>8</sup> Hart-Gonzalez and Lindemann (1993) reported language scores for 43 languages which indicate a ranking of linguistic distance from English with a range from 1 to 3, lower scores meaning greater distance. Most of the official languages of AOSSG member jurisdictions display scores of below 2, suggesting that there may exist substantial difficulties in translation.

<sup>9</sup> Legal enforcement is measured by the level of monitoring of financial statements, the power of accounting and auditing standards, and the number of personnel in the regulatory department.

**Table 4. Audit Power (Brown et al., 2014)**

Country	2002-2004	2005-2007	2008-2011
Australia	16	30	30
China	12	21	21
Hong Kong	16	22	30
India	9	11	15
Indonesia	6	8	8
Japan	12	26	26
Korea	4	14	18
Malaysia	7	9	21
New Zealand	14	20	24
Pakistan	7	10	10
Philippines	4	8	11
Singapore	13	20	20
Thailand	9	11	11

## Economic Development

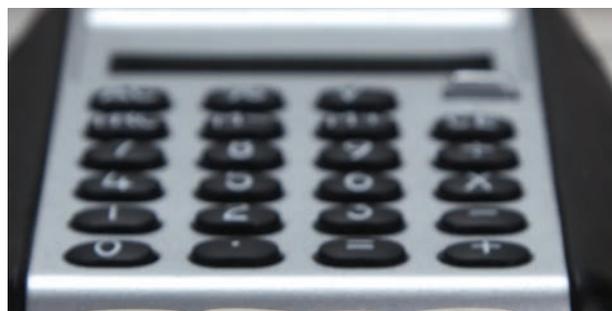
The state of economic development varies considerably within the Asia-Oceania region. Such economic disparities can lead to different levels of education systems, national standard setters' capacity, and accounting professionals' technical expertise among the jurisdictions, and in turn, give rise to inconsistent application of IFRS in the region. Thus, IFRS implementation issues deriving from differing economic development levels of each jurisdiction are yet another challenge to overcome.

## Conclusion

As noted above, the AOSSG consists of member jurisdictions with different cultures, languages, legal environments, etc. Because such characteristics of the Group can present serious challenges to adopting and applying IFRS consistently across the region, it is extremely important to understand and tackle the issues in order to successfully promote adoption and consistent application of IFRS by jurisdictions in the region.

A regional body can play various roles in this regard. In particular, it holds a key position in identifying common implementation issues experienced by the jurisdictions in the region during the adoption process; and, if necessary, communicating with the IASB or IFRS Interpretations Committee to seek solutions.

Since its inception in 2009, the AOSSG has continued to endeavor to promote consistent IFRS application within the Asia-Oceania region. Consistent application of IFRS across the region was stipulated in the AOSSG MoU as one of the



AOSSG's four major goals in 2009, and in 2011, the Group issued its Vision Paper to further clarify its goals and provide the detailed plans.

To live up to the goals it set, the AOSSG shares experience and knowledge with member jurisdictions so as to help them overcome the various implementation issues that arise during the IFRS adoption and implementation process, supporting them through a more systematic communication channel.

So far, the AOSSG has mainly focused on supporting those member jurisdictions that face difficulties in adopting IFRS due to a lack of technical expertise and support from the community through the AOSSG's IFRS Centre of Excellence in Developing Countries program (hereafter COEDC). Programs like the COEDC are vital in promoting IFRS in the Asia-Oceania region, and as the COEDC is an important project for the AOSSG now, such programs should continue further into the future.

The most crucial role of the AOSSG in the future will be to identify and resolve common accounting issues in the implementation process of IFRS in the Asia-Oceania region. Particularly, the AOSSG should explore implementation issues and the solutions by conducting joint researches and/or post-implementation reviews among countries in the region. Furthermore, the AOSSG Secretariat's function should be reinforced to facilitate effective and reliable delivery of the issues identified within the region to the IASB and/or the Interpretations Committee. It is worth noting that the issue of consistent application of IFRS is an area of great interest to not only AOSSG member jurisdictions but also international securities regulators. As the IASB chairman Hans Hoogervorst emphasised, it is important to systematically monitor consistent application of IFRS in cooperation with the securities regulators at a regional level. ■