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The post-adoption effects of the implementation of International Financial Reporting Standards in Greece

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ABSTRACT

This study investigates the effects of the transition from Greek GAAP to IFRS on the financial results of Greek listed firms. The study also examines the factors associated with the provision of voluntary IFRS disclosures before the official period of adoption, the degree of earnings management under IFRS, and the value relevance of IFRS-based accounting numbers. The findings show that the implementation of IFRS has introduced volatility in key income statement and balance sheet measures of Greek firms. Although the effects of IFRS adoption in the first year of adoption appear to be unfavourable, perhaps due to the IFRS transition costs, firms' financial measures improved significantly in the subsequent period. This result explains why in the official adoption period there is some evidence of earnings management, which is reduced in the subsequent period. The factors associated with providing voluntary IFRS disclosures before the official period of adoption include firm size and debt and equity financing needs. The study provides evidence that IFRS adoption leads to more value relevant accounting measures.

1. Introduction

The globalisation of international financial markets has increased the need for world-wide comparable accounting standards and regulation (Zarzeski, 1996). The required implementation of International Financial Reporting Standards (IFRS) by listed firms that operate in member-states of the European Union, as of January 1, 2005, should assist investors in their decision-making and enhance stock market efficiency (Botosan & Plumlee, 2002; Healy & Palepu, 2001; Leuz, 2003). At the same time, the world-wide acceptance of IFRS may indicate their high quality (Tendeloo & Vanstraelen, 2005).

Compliance with IFRS is compulsory for listed firms in Greece. Firms listed on the Athens Stock Exchange have been using IFRS since January 2005. Firms that are not listed use Greek GAAP. The transition from Greek GAAP to international accounting standards may have an effect on firms' financial results. This outcome may motivate firms to develop adjustment mechanisms to overcome potential adverse consequences of IFRS implementation (Tarca, 2004) and could lead to behaviour aimed at improving certain accounting variables, such as profitability and compensation, avoiding debt covenant violation, and reinforcing firm financial position (Weil, Fung, Graham, & Fagotto, 2006).

This study examines the impact of the adoption of IFRS on the financial performance of firms listed on the Athens Stock Exchange. This study also seeks to identify the financial attributes of firms that voluntarily abided by the requirements of IFRS before the mandated adoption date. Finally, the paper investigates whether IFRS adoption reduces the level of earnings management and enhances the value relevance of IFRS-based accounting numbers.

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The study examines the periods before and after the official adoption of IFRS. The focus of the study is on firms that adopted IFRS after 2005 (mandatory IFRS adopters) and on firms that provided voluntary IFRS disclosures before the official implementation of IFRS (voluntary IFRS disclosers). Before 2005, firms had to abide by the Greek GAAP. There was no option to voluntarily adopt IFRS before 2005. Thus, voluntary IFRS disclosers are firms that prior to 2005 used the Greek GAAP and simultaneously provided disclosures on IFRS in a voluntary manner.

The study shows that in the year of first adoption, 2005, firms tended to exhibit lower key accounting measures, such as profitability, liquidity and growth, most likely due to the fair value orientation of IFRS and the associated transition costs. In the subsequent year, firms displayed improved financial measures. The provision of voluntary IFRS disclosures before the official adoption period is associated with large size and strong debt and equity financing needs. The scope for earnings management is significantly reduced in the post-adoption period while in their first adoption year, firms tended to manage their accounting numbers in an effort to mitigate adverse results from the adoption of IFRS. The findings also show that the use of IFRS appeared to lead to accounting measures with higher value relevancy.

The remainder of the study is organised as follows. Section 2 presents the background of the study. Section 3 discusses the research hypotheses. Section 4 describes the data while Section 5 discusses the results, and Section 6 presents the conclusions.

2. Background

Studies have shown that the factors that influence the decision to provide voluntary IFRS-based disclosures include size, profitability and leverage, which are larger for voluntary IFRS disclosers (Dumontier & Raffournier, 1998; Glaum, 2000; Tarca, 2004), and international exposure and dispersion of ownership (Gassen & Sellhorn, 2006). Prior research has also shown that the use of IFRS enhances comparability and quality of accounting information, and leads to accounting harmonisation, investment growth and lower cost of capital (Barth, Landsman, & Lang 2005). Renders and Gaeremynck (2007) report that IFRS implementation is accompanied by less earnings management.

The transition to IFRS presents firms with difficulties including technical differences, the cost of change and adjustment, the time factor, and the insufficient experience and knowledge (Brown & Tarca, 2005; Gassen & Sellhorn, 2006). In addition, the fair value orientation of IFRS is likely to introduce volatility in book values and reported earnings (Andrews, 2005; Barth et al., 2005; Goodwin & Ahmed, 2006; Hung & Subramanyam, 2007), and consequently, distort the financial profile of adopting firms. These considerations may influence the financial behaviours of firms and may motivate them to redefine their strategies and decision-making processes in order to mitigate the adverse impact of adoption on their accounting numbers (Jermakowicz & Gornik-Tomaszewski, 2006).

Financial reporting under IFRS appears to provide more information about company performance (Adams, Weetman, & Gray, 1993). Countries with strong investor-protection mechanisms and regulation in place are likely to experience lower IFRS transition costs (Capkun, Cazavan-Jeny, Jeanjean, & Weiss, 2007; Lantto, 2005; Renders & Gaeremynck, 2007). Hence, the institutional background of a country may influence the effects of IFRS adoption.

The main differences between Greek GAAP and IFRS (see Grant Thornton, 2007) relate to the presentation of financial results, the readjustment of value of real estates, the accounting treatment and depreciation of certain tangible and intangible fixed assets, research and development expenditure and capitalisation criteria, pricing and evaluation of securities and financial instruments, deferred taxation, distinction between operating and financial leasing, post-employment employee benefits, provisions, consolidation criteria and methods, and accounting for goodwill and goodwill amortisation.

3. Research hypotheses

3.1. IFRS transition and financial statement effects

The study examines the impact of the transition from Greek GAAP to IFRS on the financial performance of Greek listed firms. As noted in Section 2, the implementation of IFRS would be expected to have a favourable impact on firms' financial performance and financial reporting quality. Given that the differences between the two financial reporting regimes may be substantial in terms of measurement, recognition and disclosure, the impact of IFRS adoption is likely to be significant. Also, the fair value orientation of IFRS would be expected to introduce volatility in the IFRS-based accounting numbers. The hypothesis that is tested is as follows:

H_1. The financial results reported under the Greek GAAP are significantly different than those reported under IFRS.

To test H_1, the study compares the financial results of firms that adopted IFRS in 2005 with the 2004 IFRS comparative figures that were previously Greek GAAP-based and that accompany the 2005 IFRS disclosures. The study also compares the IFRS-based financial results reported in 2005 with those reported in the post-official adoption period, 2006. This set of analyses investigates how firms have been affected by IFRS and how they have adjusted over time. The logistic regression models used are as follows.

$$RR_{i,t} = a_0 + a_1\, Size_{i,t} + a_2\, Dividend_{i,t} + a_3\, Growth_{i,t} + a_4\, Profitability_{i,t} + a_5\, Liquidity_{i,t} + a_6\, Leverage_{i,t} + e_{i,t} \quad (1)$$