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An empirical insight on Spanish listed companies' perceptions of International Financial Reporting Standards

Juan Carlos Navarro-García[a,*], Francisco Bastida[b]

[a] Technical University of Cartagena, Facultad de Ciencias de la Empresa, C/Real, n◦ 3, 30201 Cartagena, Spain
[b] University of Murcia, Facultad de Economía y Empresa, 30100 Espinardo, Murcia, Spain

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ABSTRACT

Since 2005, all publicly traded European Union companies must prepare their consolidated statements in accordance with the International Financial Reporting Standards (IFRS). This paper analyzes the consequences of IFRS adoption in a code-law country (Spain), whose context is very different from the Anglo-Saxon system. This study provides evidence on the way that environment can affect Spanish financial managers and chief accountants, when they have to prepare financial reports under high-quality standards such as IFRS. The study used a questionnaire-based survey, which was completed by 63 Spanish listed firms. The results show that IFRS are perceived as a high-quality regulation appropriate for decision-making. However, IFRS are also seen as (1) significantly different from Spanish standards, (2) troublesome, and (3) failing to meet a cost-benefit trade-off in some cases. IFRS are not considered by the survey respondents as more appropriate than Spanish standards. The results of the study indicate that statement preparers' overall views of IFRS could lead to less IFRS compliance and, therefore, lower quality financial reports than could be reached under strict IFRS application.

1. Introduction

In June 2000, a comprehensive reform of financial reporting standards began in the European Union (EU). At that time, the European Commission published "EU Financial Reporting Strategy: the way forward", requiring all publicly traded EU companies to prepare their consolidated statements in accordance with the International Financial Reporting Standards (IFRS). As a consequence, since 2005, all listed companies in the EU, including Spain, must apply IFRS when preparing their consolidated accounts (European Commission, 2000).

This paper explores Spanish publicly traded firms' perceptions of IFRS adoption. Past studies have looked at users' opinions, basically auditors and financial managers, about the adoption of IFRS in a variety of countries (Deloitte & Touche, 2003, 2004; Jermakowicz & Gornik-Tomaszewski, 2006; Navarro, Sánchez, & Lorenzo, 2007). This is the first empirical assessment of statement preparers' opinions about IFRS in Spain, a code-law country with a very different cultural and institutional framework from that of Anglo-Saxons countries. This research attempts to determine if there are factors in a code-law country such as Spain that may affect IFRS application and compliance.

As more countries adopt or consider adopting IFRS, questions arise concerning the extent to which IFRS adoption can improve financial reporting. Since IFRS are derived from common-law sources, it is not clear how this new regulation will

* Corresponding author. Tel.: +34 968 325609, fax: +34 968325782.
E-mail addresses: jcarlos.navarro@upct.es (J.C. Navarro-García), alba@um.es (F. Bastida).

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work in countries with different cultures or legal origins. Ball, Kothari, and Robin (2000), Ball, Robin and Wu (2000) and Ball, Robin, and Wu (2003) suggest that the quality of financial reporting varies among countries that have adopted IFRS. La Porta, López-de-Silanes, Shleifer, and Vishny (1998) find differences in quality, even within code-law countries, related to characteristics such as shareholders' and creditors' protection or law enforcement.

Nobes (2006) indicates that even after IFRS adoption, significant differences in international financial reporting quality remain. Therefore, previous literature provides evidence that accounting standards alone are not sufficient to achieve high-quality financial reporting.

The objective of this research is to determine the factors that may influence financial statements preparers in code-law countries to apply IFRS appropriately. A questionnaire was sent to the chief accountants and financial managers of companies listed in the Spanish market (172 firms) to determine their perceptions of IFRS implementation.

Our results indicate that financial statement preparers in Spain are satisfied with Spanish accounting standards. The respondents do not consider IFRS, in general, to be better than Spanish standards.

We find two main factors that could explain this result. First, IFRS are considered to be significantly different from Spanish standards and IFRS are viewed as more (1) complex, (2) flexible and (3) troublesome than Spanish standards. Second, negative perceptions about IFRS stem mainly from the view that adoption costs exceed adoption benefits. Respondents indicate increased reporting costs due to higher disclosure requirements and a majority predicts an increase in their firm's earnings volatility. Although the respondents acknowledge an improvement in international comparability, only a minority of Spanish firms are traded in foreign markets.[1] Although financial managers point out an increase in disclosure requirements, they do not foresee a reduction in creative accounting and perceive IFRS as less suitable than Spanish standards to limit creative accounting practices.

This study makes a contribution to the accounting literature by providing insights about the transition to IFRS by companies in a code-law reporting system. The results also show that switching standards alone is not sufficient to achieve accounting harmonization (Ball, 2001; Leuz, 2003). The study finds that acceptability and enforceability problems may prevent optimal compliance, even with standards that are considered to be of high-quality. The results should be of interest to regulators who must determine appropriate enforcement actions.

The paper is organized as follows. Section 2 presents the theoretical background and reviews the relevant empirical literature. Section 3 discusses the research questions. Section 4 describes the research methodology. Section 5 analyses the empirical results and Section 6 summarizes and presents the conclusions.

2. Theoretical and empirical background

The principal-agent theory posits that information asymmetry exists between principals (shareholders) and agents (managers) (Jensen & Mecking, 1976). Quality accounting standards, which provide guidance in preparing financial reports, reduce the impact of this information asymmetry. Thus, the better the financial reports are, the more efficient is the control the principal has on the agent. Although accounting standards are influenced by economic and political forces, economic and financial globalization requires harmonization of accounting standards internationally.

Since January 2005, publicly traded corporations in the EU have been required to apply IFRS. Previously, all Spanish firms prepared their financial statements in accordance with the Spanish Chart of Accounts (1990). Since 2005, two sets of accounting standards have coexisted in Spain: (1) Spanish regulations, used by non-listed companies, and (2) IFRS, which are obligatory for listed companies' consolidated accounts, and voluntary for non-listed groups of companies.

The main features of the Spanish Chart of Accounts (1990) are: (1) it has a strong fiscal focus; (2) it gives more importance to the legal form of the operations than to their economic basis and (3) it emphasizes accountability rather than decision-making. The accounting system in Spain, a code-law country, is a codified system that has concrete rules for financial reporting. Prior studies have analyzed the differences in financial reporting quality between common-law and code-law countries. Common-law is more market-oriented and allows investors to rely on timely public disclosure and financial reporting. In code-law countries, governments establish and enforce national accounting standards (Ball, Kothari, et al., 2000) that are influenced more by the payout preferences of agents for labor, capital and government, and less by the demand for public disclosure. Because these agents are represented in corporate governance, insider communication solves the information asymmetry between managers and stakeholders.

Studies have found that even within code-law countries, major differences exist in reporting statements. La Porta et al. (1998) place Spain in the "French family" within the code-law tradition and show that, compared to the two other code-law "families" (Scandinavian and German), "French family" countries give shareholders and creditors the weakest protection. Their results indicate that the quality of regulation enforcement reaches the highest level in Scandinavian and German countries, a medium level in common-law countries and the lowest level in "French family" countries. In Spain and other countries in the "French code-law family", preparers are not used to transparency since there is not a strong demand for financial reporting and enforcement is weak. Hope (2003a) placed Spain in last position among 22 countries regarding enforcement and disclosure.

[1] Only four Spanish firms are listed on the New York Stock Exchange, although some 30 firms are traded on OTC (over-the-counter). Furthermore, only one listed firm voluntarily applied IFRS before 2005.