Journal of Business and Economics, ISSN 2155-7950, USA
March 2015, Volume 6, No. 3, pp. 494-499
DOI: 10.15341/jbe(2155-7950)/03.06.2015/008
© Academic Star Publishing Company, 2015
http://www.academicstar.us

Academic Star

Reflecting IFRS Measurements in Corporate Financial Reporting

Cletus O. Akenbor[1], *Harvest I. Major*[2]

(1. Federal University Otuoke, Bayelsa State, Nigeria; 2. Rivers State University of Education, Port Harcourt, Nigeria)

Abstract: Globalization and development in international accounting tend to obscure the quality of corporate reporting based on GAAP and this has given rise to the adoption of International Financial Reporting Standards (IFRS). This study therefore examines how elements of financial statements are measured based on IFRS. A review of extant literature suggests that: property, plant and equipment are measured with the revaluation model; stock valuation is based on FIFO; Goodwill is based on revaluation model; depreciation of asset is reported on straight-line method; equity method is used in the measurement of equity investment; non-equity investments are reported at fair value; long-term liabilities "are valued at current debt equivalent, short-term" liabilities are reported at fair value; revenues are measured on fair value; expenses are reported at actual amount; while agriculture and mineral resources are valued at selling price. It was therefore recommended that there is dare need for proper and intensive training for professional accountants, auditors, and other preparers of financial statements to acquire relevant skills and knowledge to meet IFRS reporting requirements.

Key words: IFRS; measurement; corporate reporting; financial statement elements; GAAP

JEL codes: M

1. Introduction

Measurement is the process of determining the monetary amounts at which the elements of financial statements are to be recognized and carried to provide information about the results of management's stewardship and financial position of the firm. These measurements have been made over the decades with the Generally Accepted Accounting Principles (GAAP). But globalization in the business world and development in International Accounting of the past years brought increasingly volatility to the financial market and business and, consequently, the information needed to meet international standards and ensures market stability. This requirement is meant to address the quality and quantity of information that must be provided to local and international market participants. This calls for business entities to adjust corporate reporting in line with IFRS. According to Okoye and Akenbor (2012), IFRS is a global GAAP and a set of principles-based and globally accepted standards published by the International Accounting Standards Board to assist those involved in corporate reporting all over the world to report high quality, transparent and comparable financial statements.

Izedonmi (2011) in Awa and Abdullahi (2012) posited that the factors supporting IFRS are: continuous integration of world economy; increased interdependence of the international financial markets, absence of

Cletus O. Akenbor, Ph.D., CNA, MNAA, ACMA, Department of Accounting and Finance, Federal University Otuoke; research areas/interests: management accounting, corporate financial reporting. E-mail: akenborcletus@yahoo.com.

Harvest I. Major, MBA, Department of Accounting, Rivers State University of Education; research areas/interests: financial accounting, financial management. E-mail: akenborco@fuotuoke.edu.ng.

barriers of capital flows across national boundaries, increased mobility of capital across national boundaries, multiple listing by companies in capital market within and outside their home jurisdiction, and continuous demand by stakeholders for quality information and greater disclosure. Simmonds and Mackenzie (1992) also claimed that standardization of corporate reporting brings about minimization of accounting cost since the documentations and recording procedures are invariably the same across nations of the world, and this in the long-run leads to higher corporate profit. They added that income manipulation by foreign counterparts is equally prevented because of the strategic consistency of the standardization policy, and such prevention will bring about stability of earnings to all stakeholders of the business.

In view of the above, this paper is therefore aimed at examining the requirements of IFRS in the measurement of financial statements elements so as to provide guidance to preparers of financial statements in the conversion process to IFRS.

2. IFRS Measurement of Financial Statements Elements

(1) Property, Plant and Equipment (PPE) — These are tangible assets that have been acquired or constructed and held for use in the production or supply of goods and services. They are not intended for sale in the ordinary course of business (Alexander & Britton, 2004). IAS 16 requires that PPE should be measured and reported using the revaluation model, which may be greater or lower than cost. But GAAP recommends that PPE should be reported at cost. “For example, a firm acquired an equipment on 10th January 2010 for ₦1,500,000. On 31st December 2010 the net realizable value is ₦1,730,000”. IAS 16 requires that the equipment be reported at ₦1,730,000 while GAAP demands that the equipment should be reported at ₦1,500,000 less depreciation.

(2) Stocks — According to Derek (2010), stocks are items of value held by the firm either for use or sale. They exist in the form of raw materials, work-in-progress, or finished goods. The primary basis of accounting for stocks is cost. Cost can be determined under cost flow assumptions such as first in first out (FIFO), last in first out (LIFO) and averaged.

IAS 2 recommends the valuation of stocks based on FIFO while GAAP recommends LIFO. Consider the following transactions that relate to the purchases and issues of a stock item –

Feb. 10–purchases 200 units@ ₦10 per unit

March 2–purchases 300 units @ ₦10.50 per unit

March 11–Issues 350 units.

Stock Item I

Date	Receipts	Issues	FIFO	LIFO
Feb. 10	200 @ ₦10			
March 2	300 @ ₦10			
March 11		350	200 @ ₦10	300 @ ₦10.5
			150 @ ₦10.5	50 @ ₦10

Feb. 10–purchases 200 units@ ₦10 per unit

March 2–purchases 300 units @ ₦10.50 per unit

March 11–Issues 350 units.

Stock Item A

Date	Receipts	Issues	FIFO	LIFO
Feb. 10	200 @ ₦10			
March 2	300 @ ₦10			
March 11		350	200 @ ₦10	300 @ ₦10.5
			150 @ ₦10.5	50 @ ₦10
			150 @ ₦10.5 = 1575	50 @ ₦10 = 50
	Total stock issues		= 3575	= 3200

FIFO valuation of closing stock = 150 units @ ₦10.5 = 1575

LIFO valuation of closing stock = 150 UNITS @ ₦10 = 1500

The above illustration shows that stocks value is higher with FIFO and less with LIFO. IAS2 recommends that this stock item be reported at ₦1575 while GAAP demands that it should be reported at ₦1500.

(3) Goodwill — This is the positive different between the book value of a business or a share thereof and the amount a purchaser is willing to pay for the business or a share therein (Palmon, 2005).

Goodwill is an intangible asset and IAS 38 recommends that it should be reported using the revaluation model. For example, the balance sheet of a firm shows the value of goodwill as ₦780,000 as at 1st March, 2010. On the 31st of December 2010, the value of goodwill at revaluation was ₦650,000. Therefore, IAS 38 requires that the firm's Goodwill be reported at ₦650,000 and it should be amortized over its estimated legal life.

(4) Depreciation of assets–This is the allocation of cost of an asset over it useful life so as to match the cost against the full period during which it earns profit for the business (Couch & Baber, 2001).

IAS 36 recommends that depreciation of assets should be reported using the straight-line method. For example, a firm acquired a property at a cost of ₦180,000, with an estimated useful life of 10 years. If the residual value of the asset is ₦80,00, the annual depreciation cost of the asset will be:

$$\text{Depreciation} = \frac{180{,}000-80{,}000}{10} = \text{₦}10{,}000 \text{ per annum}$$

(5) Equity Investment — This is investment in common stock for the purposes of control. It is the residual amount of a firm obtained by subtracting total liabilities from total costs (Adedeji, 2004), IAS as requires that such investment should be reported by the equity method. This means that the investment is first recorded at cost and later adjusted each year for changes in stockholder equity of the invested. This method causes the carrying value of the investment to rise and fall with changed in the book value of the shares. For example, a firm has an equity investment of 1,000,000 shares at ₦3 per share. During the year, it earns net income of ₦540,000 and pays dividend of ₦40,000. IAS 28 requires that the equity investment should be reported at ₦3,500 (i.e., ₦3 x 1,000,000 + ₦540,000 – ₦40,00).

(6) Non-Equity Investments — These are investments in which the investor could not exercise control or influence over the financial and operating decisions of the investee company. They are assets acquired for purposes of income generation or capital appreciation without any activities in the form of production, trade or provisions of services (Palmon, 2005).

Non-equity investment could be in the form of short-term investment, long-term investment or investment properties. IFRS 5, IAS 323, and IAS 40 recommend that non-equity investment such as marketable securities and investment properties should be reported at fair value. Fair value is the amount for which an asset could be exchanged between a knowledgeable willing buyer and a knowledge able willing seller in an arm's length

transaction. For example, assume that company A bought 200,000 shares of common stock which are non-equity investment from company B on January 1, 2006 at a price of ₦2,000,000. If the selling price of the securities on 31st December 2006 is ₦15 per share, IFRS requires that the investment should be reported at ₦3,000,000, i.e., the fair value (200,000 x ₦15).

(7) Liabilities — These are probable future sacrifices of economic benefits arising from present obligations of particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events. Liabilities could be in the form of trade payables, accrued expenses, provisions and contingent liabilities (Wiecek & Young, 2010).

IAS 37 requires that liabilities should be valued at their current debt equivalent. For long-term liabilities, this implies the discounting to their present value of the future sum required to satisfy the liability. Due to materiality considerations, short-term liabilities are to be reported at face value. For example, a firm obtained a loan of ₦50,000,000 from a bank at the rate of 20% payable in 10 years. The future sum is ₦309,586,821.10. The standard recommends that the loan be reported at ₦50,751,937.89, i.e., the present value of the future sum.

(8) Revenues — Ukpai (2000) posited that revenues are inflows or other increases in the value of assets or reduction in liabilities (or a combination of both) during a period from delivering or producing goods, rendering services, or carrying out other activities that constitutes the entity's ongoing major or central operations. The amount of revenue arising in a transaction is usually determined by agreement between the firm and the buyer of the asset (Alexander & Britton, 2004).

IAS 18 requires that revenue should be reported at the fair value of the consideration received or receivable. In most cases, the consideration is in the form of cash or cash equivalents and the amount of revenue is the amount of cash equivalents received or receivable. Derek (2010) maintained that when the inflow of cash or cash equivalent is deferred, the fair value of the consideration may be less than the nominal amount of cash received or receivable. For example, sales of ₦500,000 is reported at ₦500,000. But if the sale proceed is deferred to a future date, the sale is reported at its present value.

(9) Expenses — These are inflows or other using up of assets or incurrence of liabilities (or a combination of both) during a period from delivering or producing goods, rendering services or carrying out other activities that constitute the firm's major operations. IFRS does not differentiate between expenses and losses. Any losses that are due to a firm's main business are included in its operating expenses (Ukpai, 2000). IFRS 39 recommends that expenses should be reported at the actual amount paid or the present value of the payable. For example rent of ₦1,600,000 should be reported at ₦1,600,000.

(10) Agriculture and Mineral resources–These are inventories where disposal is assured and the price is known. These inventories may be stated above cost in cases where there is no basis for cost allocation (Wiecek & Young, 2010).

IFRS 6 and IAS 41 recommend that agriculture and mineral resources should be reported at selling price. For example, agricultural produce of 50,000 units at ₦700 per unit should be reported as ₦35,000,000.

The criteria for revenue and revenue recognition under GAAP and IFRS are slightly different. The main philosophies are similar but GAAP provides more industry specific guidance than IFRS. A few of the differences lie within how cost of goods sold is determined, the operating expenses of the firm, and construction contracts (Palmon, 2005). Revenue differences in regards to construction contracts depending on the accounting method adopted, the revenue and profit for construction projects can be affected. Under U.S. GAAP, if the outcome of a project cannot be estimated, then the completed contract method is required. However, under IFRS, if the outcome

of a project cannot be estimated, revenue is recognized only to the extent of contract costs, and profit is only recognized at project completion.

Since LIFO is not allowed under IFRS, LIFO firms have to convert their inventory into FIFO terms in the footnotes of the financials. This difference is known as the LIFO reserve, and is calculated between the cost of goods sold (COGS) under LIFO and FIFO. The benefit in doing this is an increase in the comparability of LIFO and FIFO firms. However, since everything is moving towards IFRS, FIFO will be the appropriate standard if IFRS is adopted in Nigeria and this has an effect on the financial statements of the firm. In particular, during periods of high inflation, a firm that uses LIFO will report higher COGS and lower inventory as compared to a firm that uses FIFO. Higher cost of goods sold results in lower profitability and lower profits results in lower income taxes. Lower profits will also result in lower equity for the firm, which affects retained earnings in a negative way. In contrast, in a low inflationary period, the effects mentioned are reversed. Something to keep in mind for analysts converting LIFO firms to FIFO (Ross & Hicks, 2010).

IFRS does not differentiate between expenses and losses, but GAAP does. With IFRS, any losses that are due to a firm's main business are included in its operating expenses.

3. Conclusion and Recommendations

Different Generally Accepted Accounting Principles (GAAP) has been developed in various countries of the world over the past decades. The failure of this accounting framework to meet the yearnings and aspirations of financial statement users, particularly participants in the international capital markets has given rise to International Financial Reporting Standards (IFRS) in corporate reporting.

In the measurement of financial statements elements, IFRS recommends the following:

(1) Property, plant and equipment are measured with the revaluation model.

(2) Stock valuation should be based on First In, First Out approach.

(3) Goodwill should be reported based on revaluation model.

(4) Depreciation of asset should be reported on the straight-line method.

(5) Equity method should be used in the measurement of equity investment.

(6) Non-equity investments are to be reported at fair value.

(7) While long-term liabilities are valued at their current debt equivalent, short-term liabilities are to be reported at fair value.

(8) Revenues should be reported at fair value of the consideration received or receivable.

(9) Expenses are reported at the actual amount paid or the present value of the payable.

(10) Agriculture and mineral resources are valued at selling price.

Considering the above requirements, and the increasing acceptance of IFRS around the globe, we suggest that professional accountants, auditors and other preparers of financial statements should become knowledgeable of IFRS requirements through proper and intensive training so as to report transparent and high quality financial statements for better investment and economic decisions by users.

References:

Adedeji B. A. (2004). *Accounting Theory and Regulatory Framework*, Lagos.

Alexander D. and Britton A. (2004). "Financial reporting", retrieved on 5th May, 2009, available online at: http://www.newsgoogle.com/newspapers.

Awa M. and Abdullahi S. A. (2012). “Adjustment in an accounting polcy for IFRS”, *Journal of Modern Financial Management and Economics*, Vol. 13, No. 4, pp. 99-106.

Couch A. and Baber V. (2001). *Advanced Accounting and Corporate Reporting*, Dallas Texas: Aloh Publishers.

Derek P. A. (2010). “International financial reporting standards — Issues for concern”, *International Journal of Management Accounting*, Vol. 9, No. 2, pp. 87-99.

Okoye P. V. C. and Akenbor C. O. (2012). “Financial reporting framework in Nigeria and the adoption of the international financial reporting standard”, in: *20th Annual Conference on Pacific Basin Finance, Economics, Accounting, and Management*, Rutgers University, New Jersey, USA, on 8th-9th September.

Ross S. A. and Hicks C. (2010). “A new approach to corporate financial reporting”, *International Journal of Accounting, Economics and Taxation*, Vol. 7, No. 2, pp. 112-119.

Simmonds P. and Mackenzie I. (1992). “Standardization and policy consistency in accounting information”, *International Accounting Standards Papers*, London.

Ukpai N. A. (2000). *Advanced Financial Accounting Issues*, Port-Harcourt: Dokus Press.

Wiecek I. M. and Young N. M. (2010). *IFRS Premier International GAAP Basics*, Danvers MA: John Wiley and Sons.