

## The issues of the transition of accounting and financial reporting for international standards

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**Abstract:** The main purposes of this research is the justification of necessity for transition of the accountancy system to international standards of financial reporting, and scientific problem solving and working out the way of improvement of enterprises' accounting system of RK, tailored to modern conditions. The originality of research is in obtained scientific results showing the role and meaning of financial reporting formed as per IFRS as the base for managerial decision making. The problems of transition of accountancy system and financial reporting of RK onto international standards and the ways of how to solve them are examined.

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### 1. Introduction

One of the main attributes of the competitiveness of the economy is to match the accounting and financial reporting to international standards, a transition which will allow enterprises to improve the quality of management and internal control, easier access to capital, and to provide high quality, reliable and comparable information, to both internal and external users. Also, the transition will give additional impetus to the development of financial and capital markets, as both potential investors and lenders interested in providing information describing the real state of the economic activity of enterprises and gives the opportunity to assess its effectiveness in accordance with modern methods.

In the current worldwide economic crisis conditions, Kazakhstan requires significant changes in the analysis of the business of the company and improvement of accounting, as the information base for analysis is the accounting data. Therefore, first of all, all levels of management need to understand that a timely analysis of the company is a powerful tool for improving production efficiency, strengthening the competitiveness of the economy and resource-saving based on valid accounting information.

The points of theory, and methodology, and the accounting management for its further improvement in the Republic of Kazakhstan in the context of harmonization of national accounting to international standards are currently the focus of attention of scientific teams in our country.

A great contribution to the development of these issues is made by the scientists of Kazakhstan and the CIS countries and beyond :K.N. Naribaev, M.S. Yerzhanov, K.K. Keulimzhaev, A.A. Abdimanapov, A.A. Satmurzaev, K.T. Taygashinova, S.T. Myrzhakipova, F.S. Seydahmetova, Z.V. Kiryanova,

E.P. Kozlova, M.I. Bakanova, V.F. Paliya, P.S. Bezrukhih, Y.V. Sokolova and others.

However, it should be noted that a number of topical issues of adaptation of accounting to international standards are still poorly researched and remain out of view of scientific inquiry.

The main objectives of this study are to justify the need of transition of the accounting system to the international financial reporting standards, and the development of ways of improving the system of accounting firms in the Republic of Kazakhstan, which are adapted to modern conditions.

### 2. Material and Methods

In the current globalization processes it is becoming increasingly important to ensure the competitiveness of the economy of the Republic of Kazakhstan, which is the main priority in the coming period defined by the country's President. It should be noted that one of the main attributes of economic competitiveness is the matching of the accounting and financial reporting to international standards, the transition to them which will allow Kazakh companies to improve the quality of management and internal control, simplify the access to international capital, as well as providing high quality, reliable and comparable information for both internal and external users.

The current stage of the development of Kazakhstan is characterized by a gradual turn of its economy to outside world and its perception as dependent on and at the same time affecting the global economy. This defines the main directions of changes in the economic mechanism. In the accounting and financial reporting one of these areas is the use of International Financial Reporting Standards (IFRS) issued in 1973 by an independent committee with headquarters in London International

Accounting Standards Committee with headquarters in London.

Preparation of financial statements in accordance with IFRS is one of the important steps that will open doors for Kazakh entities to international capital markets. Undoubtedly, that the raising of foreign capital requires a transparency of financial information on the activities of enterprises, organizations, and management reports to investors. So long as the foreign investors will not be able to trace and be sure of the accuracy of financial statements of how the granted capital is being used, Kazakhstan will remain in a high-risk area and, therefore, will lose out in attracting financial resources from international markets compared with the other countries.

International experience shows that financial statements, formed in accordance with IFRS, are highly informative and useful for users. Use of IFRS can significantly reduce the time and resources required for the development of new national accounting rules. These standards reinforce sufficient experience in an accounting system in a market economy. They are formed as a result of hard work and research of more than one generation of accountants and accounting practitioners and researchers, and representatives of different scientific schools.

Initiation to IFRS is the most efficient and fast way to resolve the important task of domestic accounting - to create an effective system, which ensures the needs of the market economy. Therefore, one of the most pressing issues for Kazakh society is to bring the country's system of accounting and financial reporting into compliance with the requirements of the market economy and international standards. In this regard, an important role is given to the study of the accumulated experience in this field of the countries with developed market systems.

Recently adopted regulations introduced in the accounting policies new objects of accounting: intangible assets, leases, financial investments and other. Organizations are allowed to choose approaches for the reporting and valuation of accounting objects. There are international accounting principles of continuous activity, consistency of accounting policies, accruals, caution (creating of allowances for doubtful debts) and others. Presentation of financial statements has started to be close to the financial statements of western countries.

Years of work on the new regulations allow us to make some conclusions about the difficulties of their implementation and the problems that arise in

adapting the accounting and reporting of Kazakhstan to the international accounting standards.

The Government understands that the most effective way to develop the economy of our country is to implement the already recognized International Financial Reporting Standards (IFRS). In 1995 it was implemented via the development of Kazakhstan Accounting Standards (KAS) based on IFRS. It was the good work of our professionals that allowed the improving of accounting systems to a high standard. However, in its gradual development the state and society have come to realize that IFRS should be introduced more rapidly, therefore opinions about full implementation of IFRS have appeared. These ambitions have been implemented in the legislation that provides for the full adoption of IFRS financial sector from 01.01.2003, and all the rest - from 01.01.2004. The financial sector, having the most qualified staff, began its transition to IFRS. All the others, and this is the real economy, «stalled», so they postponed the transition to 01.01.2005 for public companies, and all the rest - from 01.01.2006. In the category of all other business entities were individual entrepreneurs and large businesses. Everyone understood that such subjects as small and medium businesses do not need the transition to IFRS. Therefore, in the new law on accounting of 28.12.2007, the legislator has clearly divided the subjects and determined groups that have to move to IFRS on a mandatory basis, namely public interest companies and large businesses.

From 1 January 1997, Kazakhstan joined the Anglo-Saxon model. According to many economists, the model is focused on the needs of investors and lenders, and is flexible and liberal in terms of regulation.

The Continental-European model differs by bigger regulatory activity of the accountancy system and reporting at state level and substantially depends on bank crediting.

The Continental-European model unites the national accounting systems of France, Germany, Austria and some other European countries. Essentially the national accounting system of Japan is close to this model. At the same time the Anglo-Saxon model is used in the USA, the United Kingdom, the Netherlands, Canada, Australia and some other English-speaking countries.

The main difference between the Anglo-Saxon and Continental-European models is the focus of reporting on investors and creditors of enterprises. The task of information support of state needs represented by tax authorities is put beyond the framework of the system of financial accounting and preparation of financial reporting.

A very important issue for Kazakhstan is to establish the correspondence between the rules of accounting and taxation. Constant changes in taxation force changes on the accounting system. The goal is not to change the rules of maintaining accounting records, the adoption of the Tax Code will positively affect the solution of this problem.

Another problem of the transition to IFRS is a significant difference in time between the adoption of changes to IFRS and their formal publication in the country. This creates a great inconvenience in reporting, because according to IFRS requirements of disclosing the information about the impact on the financial statements of changes of the standards introduced in the future, the newly introduced standards, and adopted and put into effect IFRIC issued by the Interpretations Committee.

One of the major problems related to IFRS is still a lack of a sufficient number of qualified personnel. This is not just about preparation of reporting, but also about the understanding and usage of it. The Chamber of Auditors of Kazakhstan in 2001 following numerous and lengthy negotiations made a decision to develop a unique program of certification of accountants and auditors. This program had to help with the transition from the former Soviet financial instruments to the international standards and give people the opportunity to improve their skills to the professional level.

Expansion of the functions performed by accounting system, introduction of trade secrets to many accounting ratios, giving accounting reporting the status of public, as well as the need to adapt the accounting and reporting of Kazakhstan to the international standards make it essential to detach from accounting two independent parts as financial and management accounting.

As it is known, the Anglo-Saxon accounting system is distinguished by high level of education of both and professionals and the whole population, which allows them to understand well a complex system of information. In Kazakhstan until recently, the accounting profession was extremely unpopular, as the accountant basically was only required to master the accounting skill. He would not be engaged with the planning and analyzing of financial and economic activities. Most of the people do not even know the basics of accounting and do not grasp accounting information.

The adaptation of the accounting and reporting of Kazakhstan to the international standards imposes new qualification requirements on accountants. Another way to improve the accounting is to increase the level of mechanization and automation of

accounting, including creating software for registration and processing of accounting data.

In the adaptation of the accounting and reporting of Kazakhstan to the international accounting standards an important role is given to the improvement of management accounting. It should include both state regulation (usually through the Ministry of Finance of Kazakhstan) and activities of public organizations such as associations of accountants and auditors, and others. In such structures, in our opinion, it is appropriate to create a department of methodology of accounting, operative consultation, education and licensing, professional conduct, departments for conference and congress organizing, departments of International Relations and Information Management.

It should be noted that the problem of adaptation of the accounting and reporting of Kazakhstan to the international accounting standards does not only depend on the output of methodological, organizational and technical issues in the field of accounting, but also on the level of development of true market relations in an organization's activity.

Under the lack of stability of the economic ties between the organizations, many of them are forced to create significant excessive inventories. This greatly complicates the assessment of inventory balances at the start and end of the period, and therefore the estimate of manufacturing resources. We should take into account the fact that under the current tax system some companies deliberately distort the accounting data that affect the volume of sales, profits, and consequently taxes. In such organizations adapting of accounting and reporting systems to international standards has become especially problematic.

The question of state regulation of the building and outlining of financial statements in the conditions of transition to market relations in Kazakhstan has paramount importance. This is due primarily to the fact that the financial report is basically a single information base for both business owners and organizations of various forms of ownership, and for all other participants in the market relations, that is third parties which have entered or are about to enter into a relationship with any organization. This raises the question of what should be the composition and content of the financial report in Kazakhstan as should they proceed only from domestic practices that have been established here in the last decade, or do we need to take into account the world experience in solving this problem?

For example, according to V.D. Novodvorsky [1], it is correct while dealing with the Provision on the financial statements to consider not only the

recommendations of international standards, but also that great historical heritage, which had been accumulated by Russia and Kazakhstan in addressing this major economic problem. According to the opinion of economists which is the same as ours, it is appropriate that into the basis of the structure of the Regulations on the financial statements would be put the Rules of public accounting (1926), which essentially correspond to current international standards. These Rules almost eighty years old were made so competently that they are still relevant today, as they affect important aspects of accounting and reporting.

Above mentioned rights consisted of the following sections:

- The subject of public reporting.
- Companies and institutions that have public accountability.
  - Reporting period of creating balance sheets and reports and their forms.
  - Information to be published, the order and timing of its release.
  - The order and timing of data to the People's Commissariat of Finance of the USSR.
  - About the supervision of the execution of the rules of public reporting.

In our opinion the written provisions are very relevant today. The work on improving accounting and reporting was done by a number of economists [2]. By our opinion they have developed successful concept of financial reporting focused on the use of international standards.

American Council on Financial Accounting Standards Board (established in 1973) in 1978 issued an official bulletin about the goals of the financial statements. The key statements of this document are to ensure that financial reporting should provide information, which, firstly, is useful to current and potential lenders to carry out rational capital investments and make a decision about investments, secondly, is understandable to those who know the economic activities and strive to study the information, thirdly, is about the economic resources of the enterprise, their requirements and influence of business transactions and events that change the resources and requirements, fourthly, is about the financial results of the company' activity during the reporting period; and fifth, helps users to estimate the amount, time distribution and probability of expected cash inflows from dividends or interest, and income from the sale or repayment of loans or securities.

The first and second tasks are faced by financial accounting information, and the third issue relates to the balance sheet, the fourth one is to the profit and loss report; the fifth one is to the statement of cash flows. Thus, the financial statements provide

information about the past to help the users in forecasting and decision-making on the future financial performance and cash flows of the organization.

For a good reason the concept of preparation and publication of reports is the cornerstone of the system of national standards in most developed countries.

Modern accounts reporting should be useful for understanding and assessing of the actual profitability of organizations, the risks associated with investments and cooperation with them, the prediction of its performance. When working on any issue related to reporting it is necessary, above all, to consider the interests of shareholders and investors, this in practice means the following. As L.Z. Shneydman [3] reasonably observes it is necessary:

Firstly, a radically rethink approaches on the consolidated financial statements preparation of which many organizations ignore.

Secondly, a change in approach to volume and composition of disclosed reporting information. According to the law «On Accounting and Financial Reporting» explanatory note should contain substantial information about the organization, its financial condition, accounting policies and significant accounting entries.

With the development of market economy in Kazakhstan financial reporting has also become an essential element of an information provision of management at all levels and the main means of communication.

As noted by M. Zadornov: «The transition or adaptation of the accounting system to the International Financial Reporting Standards (IFRS) will be gradual, and in one or two years is unlikely to actually complete the process» [4]. It is clear that transition to IFRS in Kazakhstan is quite successful, as in November 1997 the Government of Kazakhstan in its resolution confirmed Kazakhstan's transition to IFRS.

According to the approach set by the Programme of the reforming of accounting as per International Financial Reporting Standards (further - Programme of transition to IFRS), the purpose of the reforming of the accounting system is putting the national accounting system in accordance with the requirements of market economy and IFRS [5]. As seen, in this approach the transition on to International standards is not connected with the implementation of any specific macro economical tasks. In the programme of transition to IFRS the requirements of market economy to the accounting system are not defined and the fact of how the transition to IFRS could satisfy them is not reasoned. It is obvious that the transition on to international

standards cannot be the goal in itself and must assume the achievement of some economic results.

More logically defined is the approach according to which the purpose of transition to IFRS is in attracting the investments and protection of interests of foreign investors. So, by the opinion of A. Lyvshyts It is necessary to finish the least painful reforms [6], the opinion of D. Vasileva is that the reform of the accounting system has reached a deadlock [7], the transition to IFRS is the warranty of granting of external borrowings.

A.S. Bakaev, L. Gorbatova, and O. Kolesnikova think that usage of IFRS will provide the inflow of foreign investments and entrance of native economic entities on to world capital markets [8]. The same vision of benefits from usage of IFRS is appropriate for foreign experts, such as D. Damant and C. Nobs [9, 10, 11]. Theoretically the transparency of financial information defines the attractiveness of an investment object. However in scientific literature there is no evidence clearly confirming indicated fact. Therefore, at the base of such an approach to defining the purpose of transition to IFRS there is a hypothetical assumption.

By our opinion, this assumption cannot be quite applied to modern Kazakhstan conditions. According to U. Sharp the investment climate, that is the degree of favourability of the situation in the country regarding investments, is measured on the basis of a great set of indicators. For example, inflation rate, interest rates, saving ratio in GDP and so on. By the opinion of U.A. Sherbanin transparency of financial information is included in this set and is one of the significant parameters characterising investment and economical potential [12]. But in our opinion the overall and political stabilisation is a more important condition for making investment decision.

However it should be noted that the Kazakh accounting standards are not a full copy of IFRS, and it has been contrary to the expectations of western experts who have decided that their conventional standards will be mechanically transferred to the Kazakh standards. This cannot be expected because it is impossible to consider the accounting system in isolation. There is a tax system that is significantly different from those existing in Europe and the U.S. Although, it should be noted that after the amendments, it has become closer to the Anglo-Saxon system.

There is no doubt that the reform of the accounting system can be affected by objective factors and circumstances specific to the transition period of the development of country economy.

One of the main objectives of the reform process is a creation of a system of statutory regulation of accounting and reporting, which meets

the requirements of the users of financial information in the market economy and is the result of interaction of market economy institutions in the development and establishment of accounting rules and reporting [13, 14, 15].

Furthermore, the system of statutory regulation of transition economy must be a compromise between control system adequate to already established, civilized market relations, which are characterized by a high level of professionalism of the accounting and financial personnel, able to make decisions in emergency situations.

### 3. Results

The main results of the research are the following: 1) Developed of scientific-methodological and organizational and methodological basis of the accounting system for the enterprises of the Republic of Kazakhstan in the transition of accounting to international accounting standards, and 2) Determined the role and importance of accounting information in the management of enterprises' performance and validated recommendations for their adaptation to international standards, and 3) identified the issues of transition of accounting in enterprises of the Republic of Kazakhstan to the international financial reporting standards and recommended the ways of their solution.

### 4. Discussions

Thus, the system of statutory regulation of accounting system should be such that its design principles would allow it, firstly, smoothly improve by the development of economic relations in the country, and secondly, to protect the interests and needs in reliable financial information for different user groups. Reliability of the information, as well as safeguarding the interests of users of financial statements is fundamental principles in both Kazakh and foreign accounts.

Transition to accounting by the so-called accrual basis have become specific stages in the process of gradually becoming more in line with the practice adopted in countries with a market economy. In this regard the following took place: development of ideas of accounting policy, changes in accounting reporting forms, the introduction of the statement of cash flows, a new procedure for preparation of the consolidated financial statements, provision of transparency of reporting, development of the institution of an independent audit. As a result of all these changes, today's Kazakh financial statements are not very different in composition of statements prescribed by IFRS. It is difficult to distinguish between local and international practices regarding

the declaration of purpose financial statements. In both cases, it is to provide accurate information about the company's performance, useful to interested users for management decision-making. However, these statements prepared under Kazakhstan rules differ significantly from the financial information prepared in accordance with IFRS. Differences in the first place, are found in the targeted orientation of statements, reasoning of validity, representation of assets (property), usage of accrual methods, principles of prudence, the priority of content before form and rationality, and professional judgments (assessments) for reporting preparing.

In our opinion, the most important thing is to legislatively ensure the implementation of international accounting standards. If there is no legislation, and the adaptation of standards is only being recommended then these provisions will not be enforced in practice. Secondly, the lab our training process should be done in parallel with the implementation. Moreover, in addition to international certification, it is necessary to introduce own national form of certification. However as the legislation in the world now is being harmonized, then these differences will gradually fade.

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