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REGULATORY FRAMEWORK OF ACCOUNTING AND THE QUALITY OF FINANCIAL REPORTING

— *RESEARCH STUDY* —

Authors of Study

**Dejan Malinić, PhD, Blagoje Novičević, PhD
Slobodan Malinić, PhD, Rada Stojanović, PhD**

september 2016.



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- RESEARCH STUDY -

Contents

Summary (<i>Dejan Malinić, PhD</i>)	7
Introduction (<i>Slobodan Malinić, PhD</i>)	9
1. The importance of the quality of financial reporting (<i>Dejan Malinić, PhD</i>)	10
2. Causes and effects of low quality reporting (<i>Blagoje Novičević, PhD</i>)	14
3. The financial reporting environment in the Republic of Serbia (<i>Dejan Malinić, PhD</i>)	18
4. Methodological aspects of the research (<i>Rada Stojanović, PhD</i>)	20
5. Results of the Empirical Research	24
6. Key attitudes of professional accountants (<i>Rada Stojanović, PhD</i>)	34
Conclusion (<i>Blagoje Novičević, PhD</i>)	35
Appendices	39
Bibliography	44

ACCOUNTING REGULATORY FRAMEWORK AND QUALITY OF FINANCIAL REPORTING IN SERBIA

- RESEARCH STUDY -

Summary

The study of the actual situation in the field of financial reporting is motivated by the years of unsatisfactory conditions in this area, caused by frequent changes in legislation, incompliance with the relevant international regulations, incomparability of financial statements on domestic and international levels and the damages caused to investors, companies, employees, capital market, accountancy and the accounting profession, and the national economy. The regulation of the financial reporting goes beyond the capacity of individual institutions and requires the participation of a wider range of participants, such as regulators, professional organizations, academia, professional accountants and other stakeholders.

The study was based on a survey conducted among professional accountants on the existing regulatory framework and the quality of financial reporting. 583 accountants from 16 cities in Serbia participated in the survey, and the questions were answered directly in the field or by filling out a questionnaire on the website, which made it potentially available to all accountants. Answers were graded using the Likert scale of 1 to 5.

At the start of the study the targets to be achieved were set. They have been systemized as follows:

- *The review of the real situation in the field of financial reporting from the perspective of professional accountants who certainly possess the most information about the current problems, the quality of financial reports and existing information risk management;*
- *Identifying the weak points in the field of adoption of legislation, implementation of global, regional and national regulations and training of professional accountants, as well as determining the implications of all these problems on the quality of information in the financial statements;*
- *Providing constructive support to regulatory bodies in the process of adoption of new legislation, which would create the basis for the regulation of financial reporting, in compliance with the acceptable international standards.*

When it was completed, the research and analysis of the results allowed the execution of certain conclusions and accomplishment of the abovementioned objectives. Since

the results of the research are integrally presented in the study, we will mention only the key positions that are systemized as follows:

- *The quality of financial reporting is at a very low level, which is the result of inadequate legislation, frequent changes in laws and inefficient translation of IAS / IFRS and IFRS for SMEs and the accompanying regulations, which all together jeopardizes the public interest and undermines the credibility of the accounting profession;*
- *The application of widely accepted international regulations, namely IAS / IFRS and IFRS for SMEs, contributes to improving the quality of financial reporting and strengthening the confidence of foreign investors in the quality of financial statements, which increases the attractiveness of domestic companies in foreign markets and makes easier to attract foreign investors. For this reason, but also because of the possible necessity of preparing the consolidated financial statements, the option of applying IAS / IFRS should be allowed for entities that do not have a legal obligation but have an interest to do so;*
- *The increase of the number of users of IFRS for SMEs would significantly improve the quality of financial reporting in Serbia;*
- *In order to increase the degree of understandability and comparability of financial statements, as well as the rationality of their preparation, the number of normative bases for the evaluation, and the number of different forms for the preparation of financial statements, should be reduced to a reasonable level;*
- *The financial statements of companies are burdened with too many items and serious mistakes, and, as such, are completely incomparable with the financial statements required by Directive 2013/34 / EU, as well as the reports in the countries that have a long tradition in this area. In addition, inadequate deadlines for submission of these reports and the wrong priorities defined in the disclosure of these reports (giving priority to statistical needs in relation to the needs of investors) further reduce the quality of financial reporting;*
- *High quality of financial reporting requires mandatory continuous education of professional accountants and maintaining and improving their competence in order to solve complex problems in practice;*
- *Restoring confidence in the quality of financial reporting involves the signing of the financial statements by certified professional accountants, the essential acceptance of ethical codes of conduct, effective control of financial reporting and increased accountability for professional accountants.*

Bearing in mind the above findings, we are confident that they will only further reinforce the need for a much more serious approach to amend the existing legislation. Also, individual findings can be a useful landmark for addressing existing concerns in the area of financial reporting.

Introduction

Although the accounting profession has successfully developed and provided accounting services for more than a century, it still faces a number of *outstanding issues and challenges*. Dynamic changes in the overall environment, primarily caused by the globalization, are reflecting on the totality of the characteristics of the accounting profession and accounting information system.

Since the middle of the last century, the Faculty of Economics in Serbia and Serbian Association of Accountants and Auditors, *particularly taking into account the public interest*, have been dedicated to the development of theoretical and methodological accountancy knowledge and skills and to keeping pace with the constant improvement of accounting and the accounting profession. In this sense, a significant number of research studies has been realized based on the following principles: investigate, analyse, present and propose solutions, but these studies have not always been received with interest and adequate response by the appropriate regulators and tangent institutions.

The key motive and commitment to the work on this research study was based on the fact that the economic activity in Serbia takes place in the environment characterized by the unsatisfactory situation in the field of accounting regulations and the quality of financial reporting, as it is defined by the name of the study and research goals. We have investigated and presented the weaknesses in accounting regulations and, taking into account the opinion of the surveyed professional accountants, we have provided the answers on the accounting regulatory framework and the quality of financial reporting in Serbia. More specifically, these issues are placed in the spotlight and dominate the research.

For the successful realization of such goals and designated frame of research, it was concluded that the adequate research structure, which includes research, review, analysis and assessment of relevant areas, should include:

- *The importance of the quality of financial reporting*, which is essentially the analysis of the following issues: characteristics of general objectives of financial reporting, public accountability, the importance of financial reporting for investors and for the functioning of capital markets, reducing the risk of financial crisis for the economic policy makers and regulatory supervision. Special attention was paid to the quality of financial reporting for the company's management, as well as other stakeholders;
- The next segment of research was devoted to the *causes and consequences of the poor quality of financial reporting*, with a special emphasis and focus on the operational and strategic dimension of financial reporting in terms of the causes and effects of poor quality of financial reporting in the Republic of Serbia;
- The theme *financial reporting environment in the Republic of Serbia* was selected for its susceptibility to change, on the one hand, and commonly known importance of financial reporting, on the other, but also because of other disadvantages, such as the uncertainty of users in the quality of financial reporting, dysfunctional institutions, liberalization of accounting services market, etc. .;

- *Methodological aspect of the research* is a central, operational segment of the study. We have applied the methods, techniques and the survey questionnaire created by professors of the Faculty of Economics and the staff of the Serbian Association of Accountants and Auditors. The participants in the survey were professional accountants from several cities in Serbia, who were interviewed in person and via the Internet. The number of respondents was relevant, and their respective characteristics were contained in the framework of 31 questions;
- The *empirical research results* are systemized according to the given range of issues with one possible response in accordance with the gradation according to the Likert scale of 1 to 5, with first five questions and answers related to the entity in which the respondents work, their work experience, company size and legal form, with the purpose of the most adequate insight into the analysis of results;
- *Key views of professional accountants* are based on the analysed results of empirical research, systemized in nine paragraphs with the correct conclusions based on the results, on average, representing 85% of the surveyed professional accountants. The focus was on bad legal regulations, the application of accounting standards, reliability and understandability of financial statements, inadequate solutions in relation to the Chart of Accounts, and unsuitability of the financial statements for the prediction of business events, and business and financial decision-making and other poor qualitative and quantitative characteristics of the financial statements.

In the *conclusion*, the significant results of the study were once again highlighted as conclusive findings, usually placed at the end of the chapters, with the aim of potentiating important conclusions and proposals.

1. The importance of the quality of financial reporting

For many years there has been increased interest of various stakeholders around the world in the events related to the financial reporting. Increased attention is equally relevant to the investment public, management, state, regulatory bodies, professional associations and international institutions. The common interest is reflected in the efforts to raise the institutional and infrastructural quality in this area. This is particularly important for countries that have passed (or are still passing) through the process of transition, where, due to years of exclusion of corporate environment, there is not enough understanding regarding the essence and necessity of financial reporting.

According to the Conceptual Framework for Financial Reporting, issued by the International Accounting Standards Board, the general purpose of financial reporting is to provide information on present and potential investors, employees, lenders, suppliers and other creditors, which would assist them in making decisions about the purchase, sale and holding the equity and debt securities, assessment of investment security, measurement of return on investment, ability to assess fulfilment of the obligations and others.¹ It is the information that helps users to identify the financial strength of the reporting entity, changes in assets, liabilities and capital

1) *Conceptual Framework for Financial Reporting* (2010), International Accounting Standard Board.

between the periods, profitability and cash flow trends. The fact is that the financial statements are prepared primarily for investors, but it is also quite certain that they serve many other internal and external stakeholders.

Financial reporting system is an integral part of the financial infrastructure of any economy and as such provides a significant contribution to building a healthy national and international financial system. In this context, an important feature of accounting is acceptance of *responsibility to the public* in terms of quality reporting. In that respect, the accounting profession perceives investors in the capital markets, credit institutions, state institutions, business partners, employees, trade unions, various business and financial circles, regulators, rating agencies, financial analysts, investment advisers, consulting agencies, statisticians and other entities, as public. They all rely on accounting information and impartiality, honesty, integrity and professional conduct of professional accountants in the quality assurance of such information.²

Understanding the importance of financial reporting involves understanding the needs of users of financial statements. In the most general sense, the *importance of financial reporting for investors* stems from the fact that the information contained in the financial statements helps providers of capital make decisions about whether to invest, maintain their investments, or disinvest. Everywhere in the world, because of their public nature, regularity of preparation, ability to cover all business transactions in the selected accounting period and exposure to external audit, financial statements represent one of the most valuable sources of information for investors and other users. They enable the evaluation of the ability of companies to create value for the owners, the assessment of long-term and short-term financial security of the company, identifying distributable gain, assessment of readiness of companies to pay dividends, the comparison of income with income of other stakeholders, assessing the quality of management and the like. Since the decision-makers largely base their decisions on the analysis of financial statements, it is logical that they have high expectations in terms of reliability and relevance of the information contained in financial statements. In this sense, the information in the financial statements and the quality of their analysis contribute to the mitigation of information asymmetry, reducing the risk of adverse selection and the risk of abuse, as well as increasing the efficiency of capital allocation.

Financial reporting is one of the *key prerequisites for the efficient functioning of capital markets*. Information asymmetry significantly complicates the identification of good and bad companies, which significantly increases the risk of poor selection³. This results in inefficient allocation of capital, reducing the performance of enterprises and the national economy, reducing employment and slowing economic growth. We should not

2) See Malinić D., *Accounting Profession Credibility as a Factor of Capital Market Development* (2010), The 2010 Kopaonik Business Forum, „Serbia beyond the Crisis: Positioning Oneself in the Global Economy Emerging from the Crisis“, *Ekonomika preduzeća*, Serbian Association of Economists, *Journal of Business Economics and Management*, Beograd, January-February, 2010, pp. 15-28.

3) Healy, M. P., Palepu, G. K. (2001), “Information asymmetry, corporate disclosure, and the capital markets: A review of the empirical disclosure literature”, *Journal of Accounting and Economics* 31. p. 407-409.

forget the side effects in the form of smaller employee benefits, lower tax revenues and consequences for macroeconomic stability. Financial reporting, by generating publicly available information, contributes to reducing information asymmetry, making processes in the capital market more transparent and efficient, and making investors more secure. In this way, by reducing the information risks, financial reporting encourages domestic and foreign investors, increases trading volumes of securities, strengthens confidence in the capital market, and contributes to the development of this market, as well as the development of financial and private sector. All this is very important for the national economy. "Effective capital allocation process is critical to the health of the national economy, since it promotes productivity, encourages innovation, provides the efficiency and liquidity of capital markets and makes credit more accessible. Unreliable and irrelevant information indicate poor allocation of capital, which has a negative impact on capital markets and economic growth."⁴ Thus, financial reporting represents unavoidable infrastructure support to the effective functioning of the capital market.

Financial reporting is *an important factor in the stability of the financial system and reducing the risk of financial crises*. High quality information contained in the financial statements indicate exposure of the companies and investors to business and financial risks. Provided with information on risk, investors are becoming better equipped and more confident in the decision making process. In such conditions it is possible to better protect the interests and rights of creditors. The possibility of a realistic assessment of the profitability, cash flows and financial position of the company contributes to a more efficient allocation of resources and the efficient functioning of the real and financial sector, due to the reduction of information asymmetry. The risks of adverse selection and abuse are lower. In contrast, the negative consequences of poor quality of reporting and the loss of credibility of the accounting profession are low levels of trust in the financial reporting system, increased degree of caution in investors and slowing down of financial flows, which results in lower growth and reduced employment.⁵ Strengthening confidence in the institutional mechanisms that ensure the smooth functioning of businesses, increase business and financial stability and the stability of the national economy. High quality financial reporting reduces the possibility of financial fraud and the outbreak of financial scandals, which also contributes to the stability of the financial system.

Creators of economic policy can have great benefits from an analysis based on quality financial statements. It can help them in detecting early warning signals, which would enable taking the necessary actions before the crisis. Analysis of the financial statements at the level of the national economy makes it possible to identify weak points: financial and structural problems, the level of indebtedness of the economy, the problems of insolvency, the burden of financial expenses, the burden of cumulative losses and others. It can point to the (un) profitability of individual branches or particular legal forms. The analysis of financial statements can be used

4) Kieso, D., Weygandt, J., Warfield, T., Young, N., Wiecek, I. (2010) *Intermediate Accounting*, John Wiley & Sons, Ontario, p. 6.

5) See more in Maliniak, D., op.cit. pp. 15-28.

to identify the level of competitiveness of certain sectors and industries and their attractiveness to investors, but also the problems plaguing the national economy, particular sectors, industries and individual companies. Since it reveals risks and opportunities, the analysis of financial statements can be of great assistance to relevant institutions in the processes of the structural reforms, restructuring of companies in the public interest, efficient management of subsidy policies and government funding, stimulation of industries that contribute to the growth of gross domestic product, increase of competitiveness, higher level of employment and so on.⁶

Financial reporting is of *great importance for the regulators* in the capital market in the realisation of their supervisory function. This primarily refers to the regulators of the capital market, but also to the Central Bank that has the jurisdiction over the major part of the financial sector. The fact that the financial statements are primarily prepared for the investors, does not mean that regulators cannot use them. On the contrary, they are very useful, but they have to be adapted to the specific needs of regulators (for example, to control compliance with regulatory constraints, such as the maintenance of the prescribed threshold for financial institutions; to control the level of sales prices for regulated products and services; to assess risk of financial system being compromised; to counteract the effects of the financial crisis, etc.) or additional financial statements have to be prepared for the state (public) owned companies. Hence the need for the Securities Commission to be actively, at full capacity, involved in the creation of legal and professional regulations in order to fulfil the financial reporting requirements placed upon participants in the capital market. A good example of the degree of involvement of these institutions are International Organization of Securities Commissions – IOSCO and the US Securities and Exchange Commission – SEC.⁷

Finally, the information contained in the financial statements are of *great importance for the management of the company*, which has the need to analyse the financial statements of their own company to gain insight into the results achieved, financial structure, investment opportunities and prospects of the company; to assess the risks on the basis of reduction in competitiveness, liquidity, solvency, profitability, bankruptcy and so on. Management, however, also has the need to deal with the analyses of financial statements of other enterprises. The focus of management are the financial statements of business partners, suppliers and customers, in order to assess the security of production inputs and the ability of buyers to pay their obligations. Analysis of competition is necessary for assessing the strategic competitive position of enterprises, and for the implementation of benchmarking in order to identify opportunities for performance improvement. The investment of surplus cash requires the assessment of the attractiveness of securities of quoted

6) Malinić, D., „Mogućnosti i rizici ocene performansi privrede Srbije na osnovu analize finansijskih izveštaja“, Računovodstvo, Savez računovopra i revizora Srbije, 1/2016. str. 7-37.

7) See more in Robinson, T. R., Henry, E., Pirie, W. L., & Broihahn, M. A. (2015), *International Financial Statement Analysis*, John Wiley & Sons, Inc., New Jersey, pp. 99-104.

companies, which allows avoiding investing in high-risk enterprises and directing investment into securities that can bring high returns.⁸

If we bear in mind the enormous importance of financial reporting and the number of decisions that different interest groups are basing on the financial reporting, it becomes understandable why the users of these information are very sensitive with regard to their quality. Regularity of reporting, public nature and responsibility of accountancy and accountants to the interests of the public, make this information different from the rest. High quality financial reporting, from the perspective of investors, represents the ultimate requirement. Hence *the enormous obligation and responsibility of the state and the competent regulatory bodies to create a legal framework that will provide conditions for quality financial reporting*. The liberalization of markets and the need to attract foreign capital make inevitable the need for the harmonization of financial reporting with global (International Accounting Standards - IAS and International Financial Reporting Standards - IFRS) and regional regulations (EU Directive). We could say that the improvement of the very poor situation in this field is the national interest.

Considering the importance of the quality of financial reporting, we can conclude that the efforts of the legislator (quality legislation) and the accounting profession (quality professional regulation) are needed to provide true and fair financial statements. Those *responsible for the quality of financial reporting* at the national level are the state, the national regulatory bodies, professional organizations and the independent public oversight bodies, while at the corporate level responsibility is borne by the management, the audit committee and professional accountants (including auditors).

2. Causes and effects of low quality reporting

High quality financial reporting in countries with a developed culture of financial reporting, to which the Republic of Serbia aspires, implies an adequate legislative and regulatory framework, as well as relevant institutional framework for the development of human capacities and the continuous construction of other capacities and processes, as well as adequate presentation of financial statements, their consistency and comparability. None of these important factors of financial reporting in Serbia is working satisfactorily. The quality of the financial reporting in the Republic of Serbia is poor because of the following reasons, as reflected in the following:

- a) it is not compliant with Directive 2013/34 / EU and Regulation 2002/1606 / EU of the European Union. The compliance with international professional regulation is only partial, because the entire corpus of regulations is not available in Serbian language (there are no officially translated interpretations of standards, education standards, quality standards, a code of professional ethics, etc.), and because the versions of IAS / IFRS that are in effect do not correspond current IASB versions of the standards due to

8) Malinić, D., „Mogućnosti i rizici ocene performansi privrede Srbije na osnovu analize finansijskih izveštaja“, op. cit. str. 7-37.

- inefficiency in translating or non-translating, and delays in the implementation of the international professional regulations;
- b) the regulatory framework of financial reporting of the Republic of Serbia include domestic legislation in the form of a *Rulebook on the manner of recognition, measurement, presentation and disclosure of items in the individual statements of micro and other legal entities* with regard to the private sector, and Regulation on Budget Accounting Public Sector, which is mainly used in very underdeveloped financial reporting practices;
 - c) the financial reporting system is extremely unstable; in the period from 2002 to 2013, the law related to accounting has been changed 3 times, and during the last 27 years, 6 times, not including the additional amendments during this period, which in developed cultures of financial reporting is not a sufficient period for a single change to be fully implemented. This approach threatens the comparability of financial statements in the international context;
 - d) the ethics for professional accountants, as the foundation of modern professionalism for the majority of members of the profession is ignored, and only is mentioned the ethics of auditors, as professional accountants par excellence, who comprise a much smaller number of members of the profession, which is contrary to the IFAC Code for Professional Accountants. Accordingly, there are no regulatory obligations, no disciplinary actions nor education as an inseparable part of their development;
 - e) the financial reporting system involves the establishment of institutional responsibilities and coordination of the activities related to financial reporting, as well as the existence of professional accounting organizations. Institutional responsibility for financial reporting is generally linked to the government - the Ministry of Finance - in spite of the fact that the Government, by its nature, cannot be in this position, because it is in conflict of interest. The institutions for coordination, in the true sense of the word, do not exist, because the National Commission for Accounting and Public Oversight Committee are not what they are supposed to be. The institutionalized National Commission for Accounting only monitors the process of implementation of European directives in the field of accounting, and IFRS and IFRS for SMEs, while the real coordination between stakeholders in the financial reporting process in general is not present. Similarly, the institutionalized *Public Oversight Board, as an independent body responsible for matters of financial reporting does not deal with, nor can address these issues because it has no jurisdiction over sanctioning the substandard work in the financial reporting process. In addition, the sufficient illustration of its independence is the fact that out of 7 members, 5 members are appointed by the Government. Professional organization - Serbian Association of Accountants and Auditors, de facto "preserves" quality of financial reporting and protects the public interest, modelled by professional organizations in developed cultures of financial reporting, in accordance with the nature of its activities and assumed membership obligations to international organizations and professional bodies. However, it is not formally institutionalised, which means that there is no natural guardian*

of the financial reporting quality and the public interest. Chamber of Auditors, which is institutionalized as a professional organization cannot actually act as such because it is strongly influenced by the Government;

- f) Without formal institutionalization of independent professional organization there are no quality professional accountants, including auditors. The professional organization has the task to carry out a general assessment of the human accountancy resources, to conduct professional training of accountants, to develop their professional skills, assess their competence and work on their continued development. In this context, the construction of capacities and processes, which is related to the adopted national strategy and action plan, loses all meaning;
- g) the form and substance of the current financial statements, as carriers of information about the financial position, performance and changes in financial position in the Republic of Serbia, are not theoretically based or compliant with European directives on accounting, IAS/IFRS, or with any developed national practices of financial reporting. Specifically:
 - There are 236 items in balance sheet and income statement, as opposed to 88 in the EU and 67 in IAS/IFRS. Thus, these financial statements have become opaque and hard to read, and therefore non-transparent, as well as fully internationally incomparable;
 - the purpose of financial reporting for economic judgment and decision-making of all users of such reports is completely ignored, except for National Statistics, provided that these are the same reports. It is generally accepted practice that annual financial statements are submitted by the end of February for the previous year. In our legislation, this is the date when the financial reports for statistical purposes have to be submitted, while regular annual financial statements for other purposes should be submitted by the end of June for the previous year, and they should be publicly available no later than 31 October for the previous year with a possibility of replacement of financial statements until the end of the year for the previous year;
 - The primary qualitative characteristics of the information contained in the financial statements - reliability and relevance, have been compromised. Balance sheet, income statement and statistical report on performance prepared for statistical purposes do not have to be the same as the regular annual financial statements, because there is no explicit mechanism to guarantee that. In addition, the current legislation gives the possibility of replacing the financial statements by the end of the year for the previous year, which is difficult to explain;
 - Financial statements contain incomplete, often false, inconsistent and partial information, and a large number of entities do not submit financial reports at all.
- h) Bookkeeping and preparing financial reports is carried out with the use of numerous, mutually different, non-standardized accounting programs, which often provide opportunities for manipulation, abuse and creative accounting. Standardization of the use of information technologies in accounting (which was initiated by the Accounting Act of 1993 based on

standards JRS -33- Accounting software, issued by Serbian Association of Accountants and Auditors) would contribute to increasing the quality of financial statements and restoring confidence in them. Also, all electronic documents should be created according to the standard ebXML (OAZIS), i.e. ISO 15000. Furthermore, electronic records should be established according to the security standard ISO 27000. The accounting regulatory framework should recognize the global trends of the standardization of transmission and exchange of business information and in accordance with contemporary experiences of countries with a developed culture of financial reporting and the recommendations of the International Federation of Accountants, it should include the international standard for the electronic exchange of business information XBRL.

*Financial reporting in the Republic of Serbia has all the characteristics of the poor quality of financial reporting and the **consequences** are:*

- the business environment is totally compromised, market risks are very significant, instability of the financial system has been induced and investor confidence has been undermined, and therefore there are no conditions for the establishment and development of market economy nor efficient and reliable capital markets and crediting, and thus no conditions for taking advantage of globalization, with increasingly difficult integration into the European Union on the basis of the best possible use of resources. The information asymmetry has deepened, which leads towards poor selection of investments and the negative impact on economic growth through the omission of better alternatives;
- the protection of the public interest as the basis of stable growth and development of economy and society has been compromised, because the growth opportunities and growth itself are not adequately measured, and the achievements and opportunities for development are not adequately assessed and evaluated, and the productivity in economy has been decreased;
- there are no conditions for the reduction of numerous accounting scandals, as well as for combating fraud and corruption, while the emergence of poverty and uneven distribution of national wealth is being encouraged;
There is a lack of adequate information base for corporate governance and the probability of occurrence of the bankruptcy risk has significantly increased;
- the work of commercial and other courts has been impeded.

Thus, there are many negative consequences to poor quality of financial reporting in Serbia; the assessment of the financial position and performance of the business system in both private and public sector, as well as the economy as a whole, is significantly restricted; the financial statements are incomparable, incomprehensible and unreliable because of the absence of the ethical component and obligatory certification obligations of persons who assemble them, and as such are a good basis for the violation, manipulation and gray economy. It is practically impossible to predict the future and recognize the business risk on the basis of low quality financial statements, which hampers investments and capital market development. In a word, financial reporting is reduced to a formal legal obligation to prepare and submit financial statements.

3. The Financial Reporting Environment in the Republic of Serbia

The accountancy profession has never been independent of the society in which it develops. The same is true for financial reporting which has partly been influenced by world tendencies in this area, but to a much greater extent by the immediate environment in which it is applied. The environment includes conditions, limitations and effects of socio-economic, political and legal nature that are subject to change over time.⁹ In the last twenty years or so, financial reporting environment has suffered significant changes at the global level. Globalization of markets for goods and services, internationalization of capital markets, changes in the structure of the economy towards increasing importance of the economy based on knowledge, exhaustive commitment to the full implementation of fair value before and reviewing such attitudes after the financial crisis, major financial scandals and undermined credibility of the accounting profession are only some of the events that have left marks in the financial reporting system. In Serbia, as one of the few countries that have not yet completed the process of transition, numerous problems are still present that prevent the creation of a regulated and sustainable financial reporting system in the long run. In this sense, we must bear in mind a few important facts.

- Not even in Serbia do requirements related to the harmonization of financial reporting at the global level have a viable alternative, despite some attempts to marginalize such processes. At the global (world) level, this means the application of internationally accepted professional regulation in the financial reporting process. Vision of global international accounting standards has been publicly supported by the important international institutions such as the G20, the World Bank, the International Monetary Fund (IMF), the Basel Committee, International Organization of Securities Commissions - IOSCO) and the International Federation of Accountants (IFAC). Not including the countries that are in the process of transition to IFRSs / IASs, today 119 of the world countries require the application of IFRSs / IASs to all companies, or, for the most part, to public companies and financial institutions.¹⁰
- The intention of Serbia to join the European Union places additional requirements before the regulators of financial reporting relating to the *mandatory harmonization of national legislation (hence, the accounting regulations) with the EU acquis*. This further complicates the process of international harmonization, since there are differences between the global professional regulations and EU regulations (despite the existing convergence of EU directives with IFRSs/IASs). However, these differences are not insurmountable. Much bigger problem lies in the missed opportunity to incorporate the EU legislation in the previous laws, which implies a new amendment of regulations and additional high costs that could have been avoided.

9) Kieso, D., Weygandt, J., Warfield, T., Young, N., Wiecek, I. op. cit. p. 4.

10) See more at: <http://www.ifrs.org/>, retrieved on September 10, 2016.

- *The fundamental lack of understanding of the significance of financial reporting* and its reduction to a formal obligation of submitting financial statements on a particular day, is probably the biggest problem and obstacle to the arrangement of financial reporting in Serbia. This is sufficiently supported by evidence of ignoring international practices in the preparation of financial statements as basic instruments of business communication, numerous omissions in the existing regulations, bias in the selection of some legal solutions and institutional disregard of the fact that in 2014 more than 24,000, and in 2015 more than 30,000 companies did not submit financial statements. Such an attitude towards financial reporting undermines the confidence in the financial statements and causes a long-term damage to the national economy. The neglect of public interest significantly complicates the process of arrangement of financial reporting.
- *Instability of regulation and uncertainty of accounting information users* are identifiable characteristics of the business environment. In the course of twenty years in Serbia (from 1993 to 2013, when the latest laws on accounting and auditing were passed) five laws on accounting were passed, each accompanied by materially different forms of financial statements, which are usually formally and fundamentally incomparable. This is more than a sufficient reason for a review of the role of the individuals involved in the process, as well as the institutions (not only domestic) which have accepted such solutions. The European Commission assessment that further efforts are needed to achieve compliance with Directive 2013/34 / EU, speaks volumes about the current regulations.¹¹
- *Fragmentation and disregard of the key participants* in the overall chain of financial reporting gives a special touch to the environment where the financial reporting system needs to be regulated. Overcoming such a situation is a necessary precondition for the creation of high-quality financial reporting system. This requires the neutralization of the effects of different stakeholders that have inflicted enormous damage to both the profession and the national economy by abusing such a condition.
- *Inadequately established and dysfunctional institutions* which ought to have the role of ensuring the quality of required financial reporting further complicate the necessary arrangement of the financial reporting system. Hereby, we primarily think of the National Commission for Accounting which should be competent for the development of the financial reporting system and the Public Oversight Board of Audits. In the case of the National Commission, key issues are related to the derogation of the statutory responsibilities and accountability of this body and the lack of criteria to ensure an independent and competent Board composition. The Public Oversight Committee was established as a public authority, which, according to the European Commission, threatens its independence. In addition, the Committee does not have adequate powers, instruments of action, nor the necessary infrastructure, since technical

11) European Commission (October 2014), Serbia Progress Report, *Accompanying the Document: Enlargement Strategy and Challenges 2014-2015*, Brussels, October 2014. p 26.

assistance is provided by the Chamber of Auditors, which, itself, is subject to control¹². In the very base of strong institutions lie independence, competence and credibility, which are now lacking.

- *A complete liberalization of accounting services markets*, in the sense that accounting activities, as well as public interest activities, can be conducted by anybody, regardless of education, in itself indicates the quality of financial reporting we can expect, as well as the attitude of the legislator towards quality. The rationale that it is a corporate decision in underdeveloped countries is not good enough as in the countries with a strong accounting tradition and culture. Carefully differentiated approach to the problem of certification of professional accountants is necessary in order to protect the public interest. A positive selection for entering the profession must be in place, as well as mechanisms to eliminate all practitioners who violate the laws and ethical rules of the profession.
- The conclusions regarding the necessity of further development of the accounting aspects of modern information and communication technologies, particularly in terms of binding regulations and the quality of financial reporting, such as: losing pace with the global process of digitalisation of financial reporting in terms of the regulatory framework and the positive impact on the quality of financial reporting, speed, accuracy, and cost savings related to the process of preparation, presentation, and in particular, the use of financial statements.

The above features of the current environment which requires the regulation of the financial reporting system clearly indicate that to achieve this goal, we must create a stimulating environment that will allow it. Otherwise, instability of regulation and uncertainty of protecting the interests of key stakeholders, including the government, will persist.

4. Methodological Aspects of the Research

Data collection for the research relating to the accounting regulatory framework and financial reporting quality was done by applying the method of empirical research - examination method. Within the examination method *survey* was applied as a research technique in the narrow sense, in the form of collection of written data on the attitudes and opinions of a representative sample of respondents by means of a questionnaire.

Survey. The survey questionnaire was delivered on site and was available on the website of the SAAA, to the respondents who individually provided answers to the questions. The survey was anonymous, the closed-type questionnaire was provided in the form of Likert scale of 31 questions, containing the instructions for completing the list of possible answers. The possible responses range from a completely negative attitude, through neutral, to a completely positive attitude in each single question on a scale of 5 categories of attitudes (strongly disagree; disagree, mainly agree, agree to a large extent, and fully agree), and required only one answer. Respondents were given information on the purpose of research, the method of the sample selection, and were acquainted with the fact that the survey is anonymous.

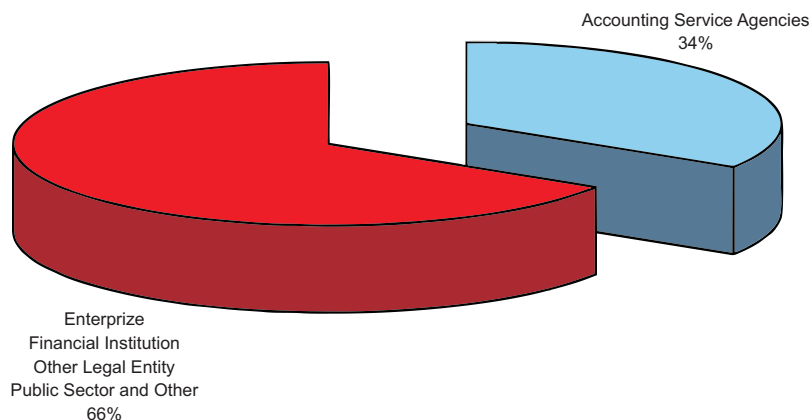
12) Ibid.

The study involved professors of faculties of economics and advisors - expert professionals who created the questionnaire and analyzed the survey results (1); professional accountants who have completed the survey sheets and whose attitudes are the subject of the research (2); and SAAA technical staff who distributed the questionnaire and provided information about the purpose of the survey, collected the completed survey sheets and conducted aggregated processing of the results (3).

The survey was conducted in the period from 16 to 30 June, 2016, in 16 cities in Serbia: Subotica, Nis, Pozarevac, Pirot, Sremska Mitrovica, Vrsac, Novi Sad, Sombor, Kragujevac, Pancevo, Backa Palanka, Zrenjanin, Novi Sad, Belgrade, Krusevac and Kikinda. Simultaneously, a part of the research was carried out by means of survey on the Internet. The territorial dispersion and differences in the level of development of the economic activities of these cities, i.e., the differences in the requirements of financial statement users that comprise the professional accountants surveyed contribute to the relevance of the research results.

Sample. The study sample consists of 583 professional accountants, who are employed in companies, financial institutions, other legal entities, the public sector and other (66%) i.e., in an agency for the provision of accounting services (34%). Sample characteristics associated with the engagement and working experience of professional accountants surveyed, as well as with the size and legal form of the reporting entities where the surveyed professional accountants keep business records are illustrated below.

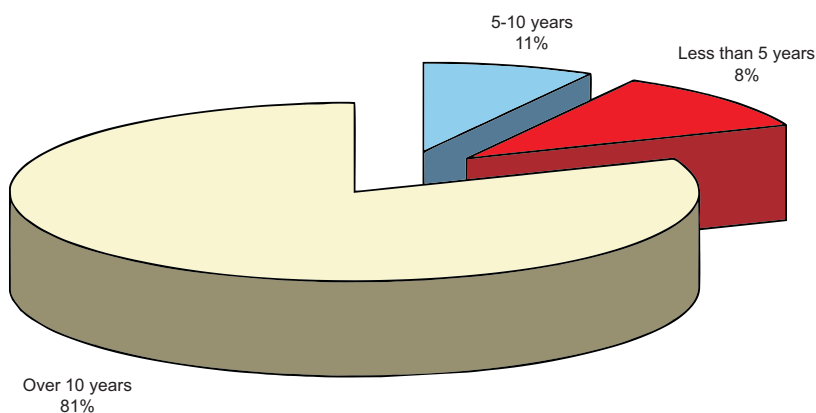
Engagement of professional accountants surveyed



The sample was intentional, because there is a reasonable expectation that the professional accountants who have acquired professional titles are motivated and interested in the quality of regulatory framework that applies directly to their work, and in the quality of financial reporting of which they are the main carriers, as well as that the attitude they express on these categories will be respected.

Work experience of professional accountants surveyed is over 10 years (81% of the survey participants), from 5 to 10 years (11% of the survey participants) and less than 5 years (8% of the survey participants).

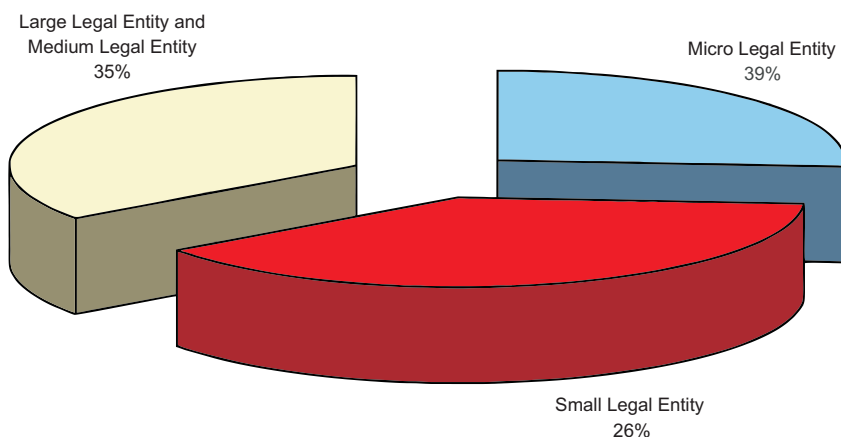
Work experience of professional accountants surveyed



The fact that over 80% of respondents, has over 10 years of experience indicates their competence to express their position on the characteristic of the accounting regulatory framework and the level of financial reporting quality.

Regarding the size of the legal entity for which the surveyed accountants keep business records, 35% of accountants are engaged in large and medium-sized legal entities, 26% in small legal entities and 39% in micro legal entities.

Size of reporting entities for which the surveyed professional accountants keep business records

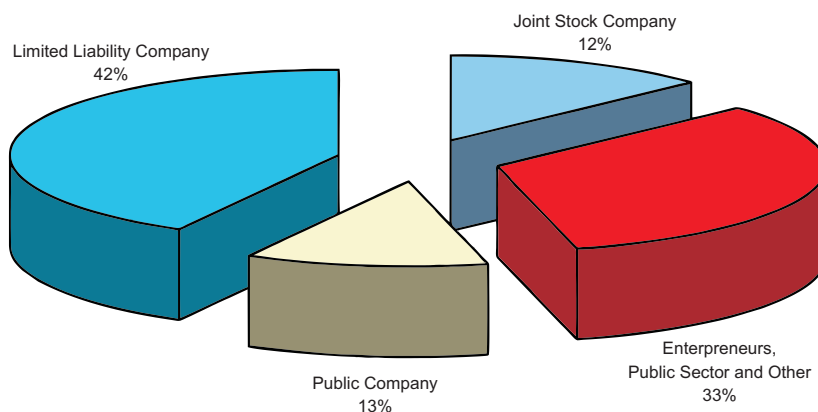


Since the surveyed professional accountants prepare financial statements for all the structures of legal entities in terms of their classification by size, there is no doubt in their familiarity with all aspects of the regulatory framework, as well as the prescribed forms of financial statements.

In terms of the legal form of reporting entities for which the surveyed accountants keep business records, limited liability companies are represented with 42%,

joint stock companies with 12%, public companies with 13% and other types of organizations (entrepreneurs, public sector) with 33%.

Legal form of the reporting entities for which the surveyed professional accountants keep business records



The fact that the surveyed professional accountants prepare financial statements for different organizational forms of business entities: limited liability companies, joint stock companies, public companies-entrepreneurs as well as for the public sector, indicates a reasonable expectation regarding their awareness about the content of the legal accounting regulations.

Specified characteristics of the sample on which the study was conducted should provide reliable, credible, accurate and relevant information, i.e., the size and heterogeneity of the sample structure confirm its representativeness, as well as the relevance of the results of the research conducted.

Processing and interpretation of the research results. Arranging and processing the data after the conducted research is carried out in the form of statistical and descriptive interpretation. Functional analysis is applied to the collected data, based on which relations within the scope of the research are conceived, as relations between the subject of research and the environment. Total measure in the scale of attitudes, which is a measure (intensity) of attitude is formed as a composite of responses to single statements, or by means of summation of responses in relation to the items on single questions of the questionnaire a total score is formed as a composite indicator for the specific question (summation scale).

In the course of data processing multivariate factor analysis was also used, as a method of multidimensional analysis that is used to describe the interdependence of a large number of variables. Factor analysis enables the identification of features not directly visible, as well as effective extraction of information from the overall database and identification of sets of related data in order to adequately review the data structure.

5. Results of the Empirical Research

Employed

471 of 583 answered this question

1	at a company, financial institution, etc.	313 / 66%
2	at an agency that provides accounting services	158 / 34%

Work experience

545 of 583 answered this question

1	Over 10 years	443 / 81%
2	From 6 to 10 years	62 / 11%
3	From 1 to 5 years	37 / 7%
4	Less than one year	3 / 1%

Size of company

523 of 583 answered this question

1	Micro	204 / 39%
2	Small	138 / 26%
3	Medium	97 / 19%
4	Big	84 / 16%

Legal form of the company

522 of 583 answered this question

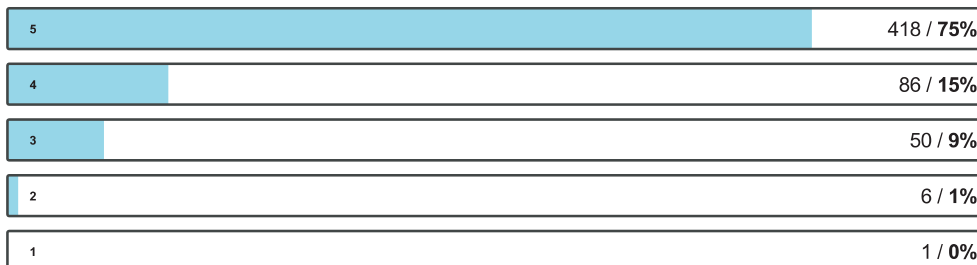
1	Ltd.	219 / 42%
2	Other	172 / 33%
3	Public-owned	66 / 13%
4	. Joint stock	65 / 12%

Implementation of IFRS and IFRS for SMEs requires stable and quality professional regulations (without frequent changes)

561 of 583 answered this question

Average: 4.63

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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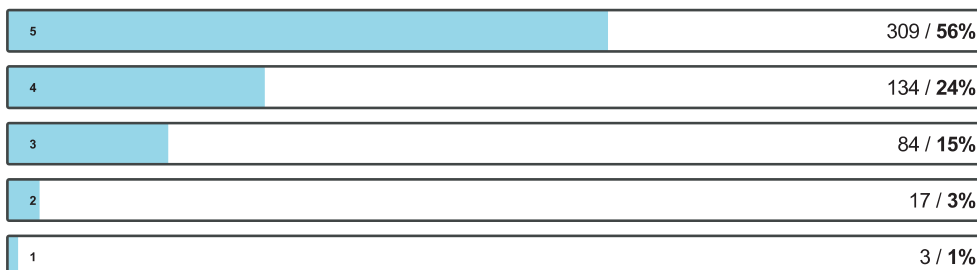


A high number of bases on which balance sheet items are valued, does not contribute to the reliability of reporting, while it increases costs and demands more effort from the accountant

547 of 583 answered this question

Average: 4.33

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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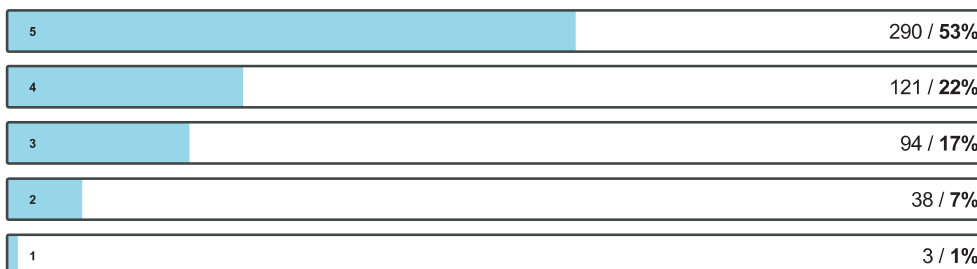


The existing financial statement forms, because they are too big and contain errors, do not serve their purpose

546 of 583 answered this question

Average: 4.20

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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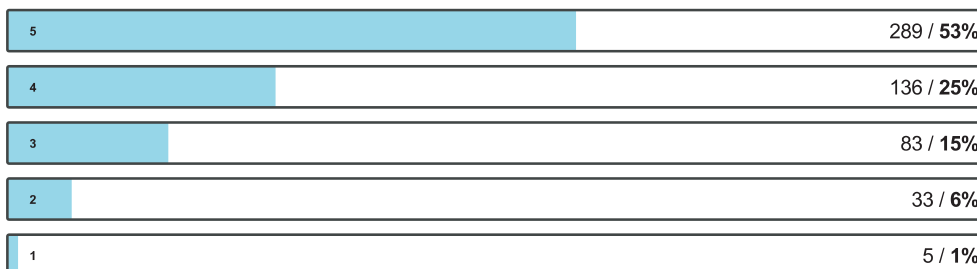


If the scope of financial statements is decreased, there would no longer be need for special forms of financial statements for particular reporting entities

546 of 583 answered this question

Average: 4.23

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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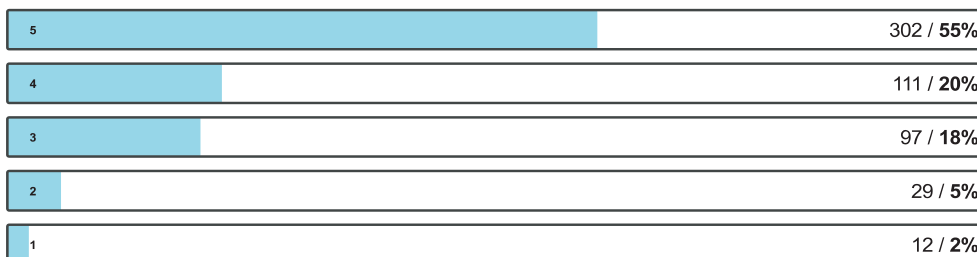


All entities, regardless of their classification, should be allowed to apply full IFRS, which would result in the decrease of the amount of work, number of mistakes, and costs of transmission from one category of classification to another, as well as with consolidation

551 of 583 answered this question

Average: 4.23

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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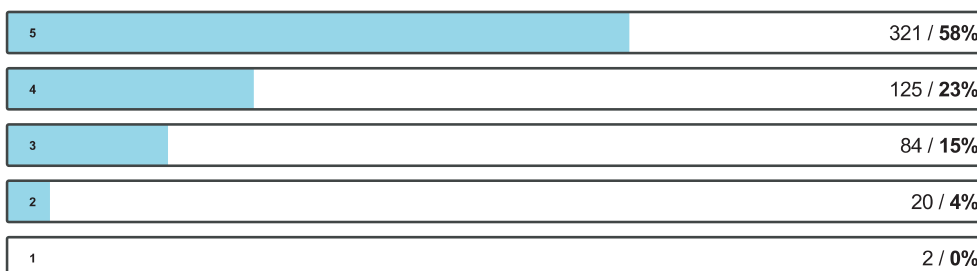


The lack of updated translations of IFRS, IFRS for SMEs and supporting regulations hinders the qualitywork of accountants and auditors

552 of 583 answered this question

Average: 4.35

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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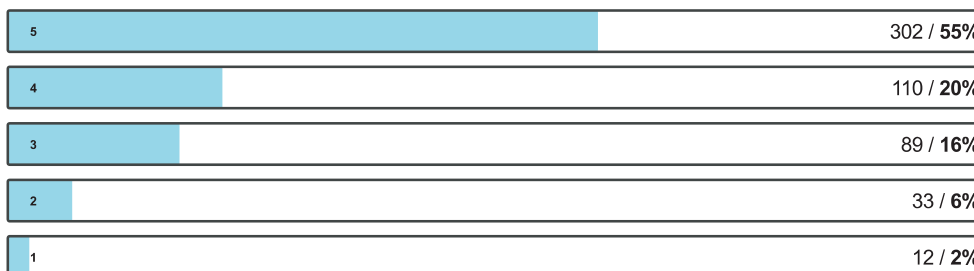


Single entry bookkeeping should be regulated in more detail and reduce this possibility to the entrepreneurs with no more than two employees and with modest turnover

546 of 583 answered this question

Average: 4.20

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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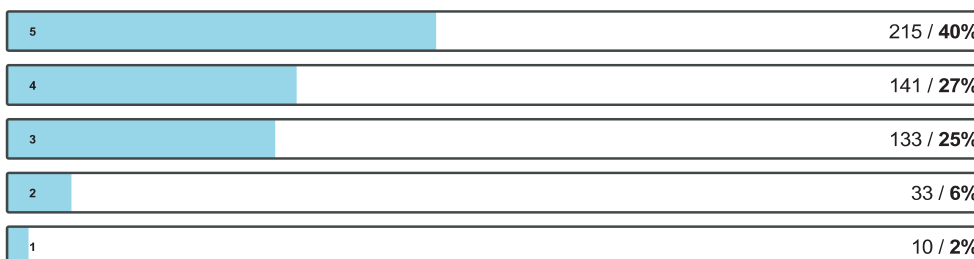


The rulebook for the valuation of items for micro and other entities does not provide all the necessary information for the recording of operational changes, without the usage of IFRS for SMEs

532 of 583 answered this question

Average: 3.97

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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Since the IFRS for SMEs is in use, there is no need for the special rulebook for micro and other entities

532 of 583 answered this question

Average: 3.96

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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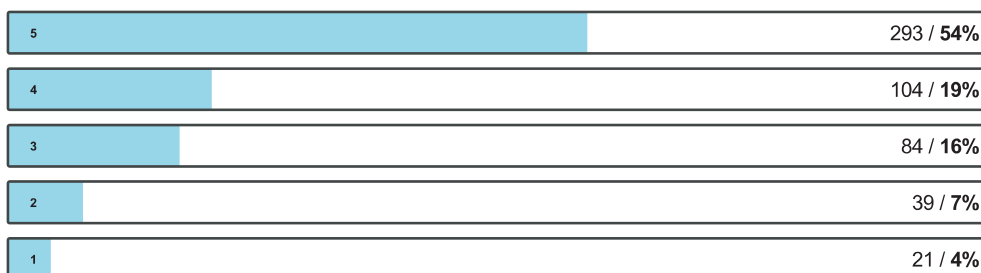


Other entities should not be separated either by financial statement forms or by chart of accounts

541 of 583 answered this question

Average: 4.13

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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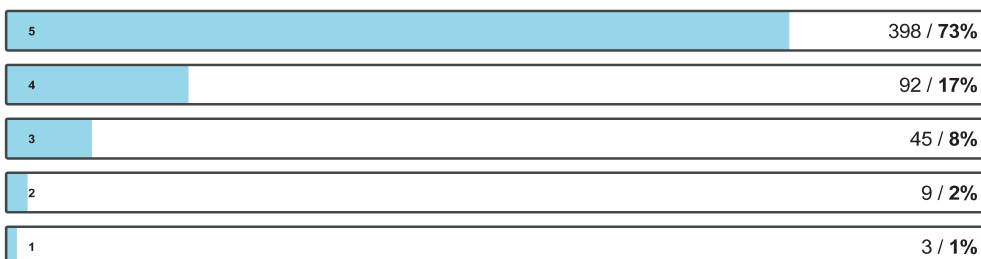


The existence of 13 charts of accounts makes it more difficult for the accountant to do his or her job, because the balance sheet positions in all entities have the same essence and terms of recognition

547 of 583 answered this question

Average: 4.60

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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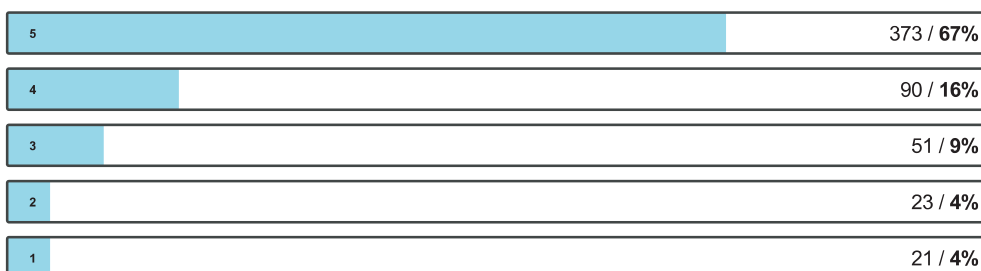


Regular financial statements should be submitted on February 28 (29), and they would be used for statistical purposes

558 of 583 answered this question

Average: 4.38

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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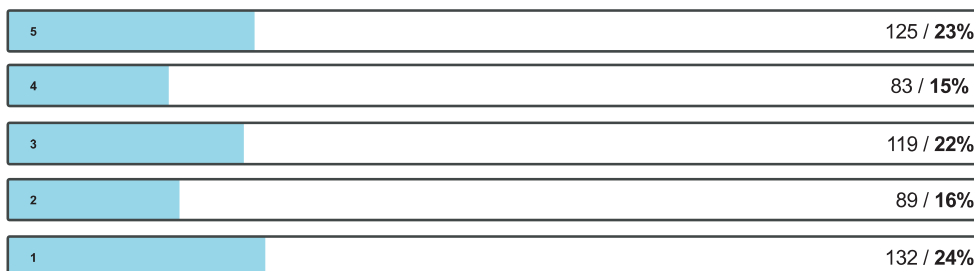


The possibility of replacing financial statements should be abolished

545 of 583 answered this question

Average: 2.96

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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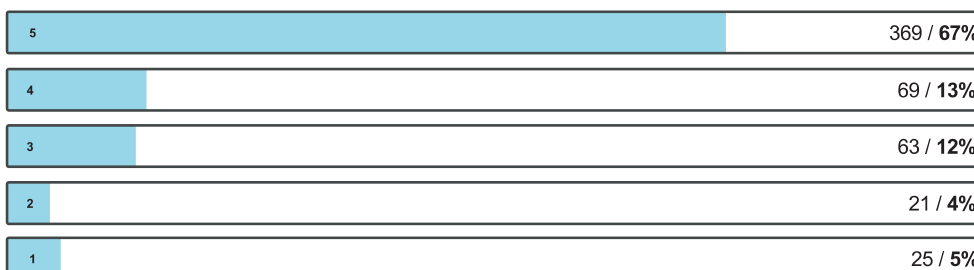


The signing of financial statements by certified professional accountants who possess the required knowledge and skills, would restore faith in the quality of financial statements

547 of 583 answered this question

Average: 4.35

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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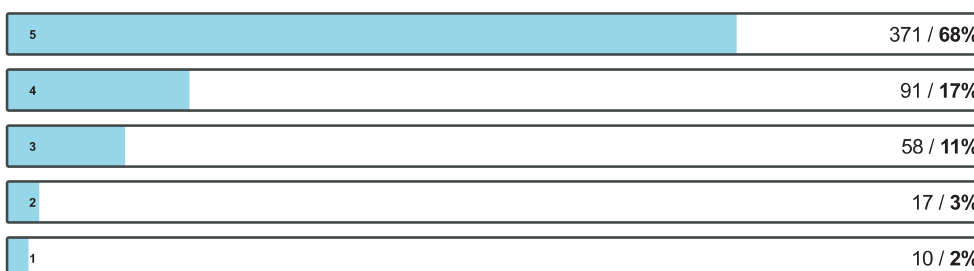


The return of education standards and Code of Ethics for professional accountants in legislation would contribute to the reliability of financial reporting

547 of 583 answered this question

Average: 4.46

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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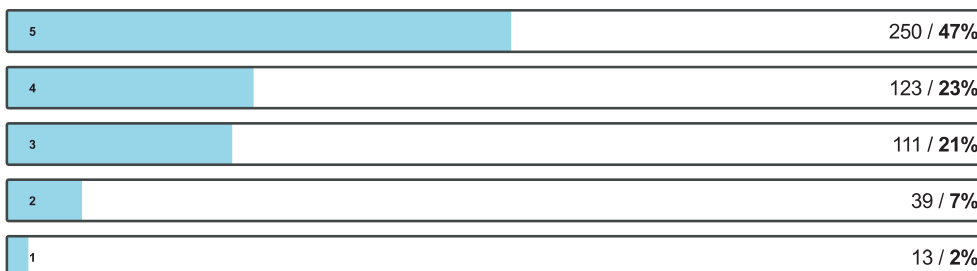


The control of financial statements is at a very low level, which contributes to gray economy and corruption

536 of 583 answered this question

Average: 4.04

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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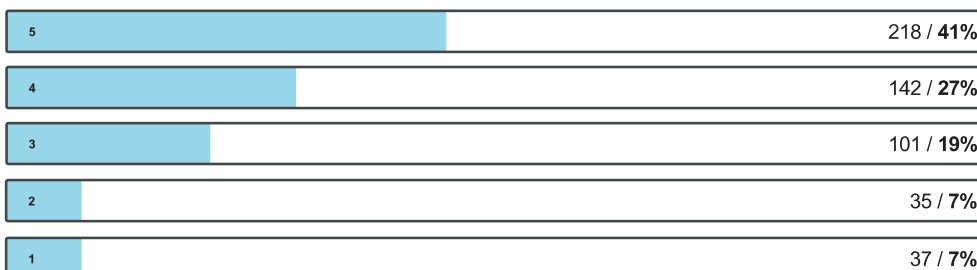


By introducing the accountability of the providers of accounting services, the state would have an insight into tax collecting on that grounds

533 of 583 answered this question

Average: 3.88

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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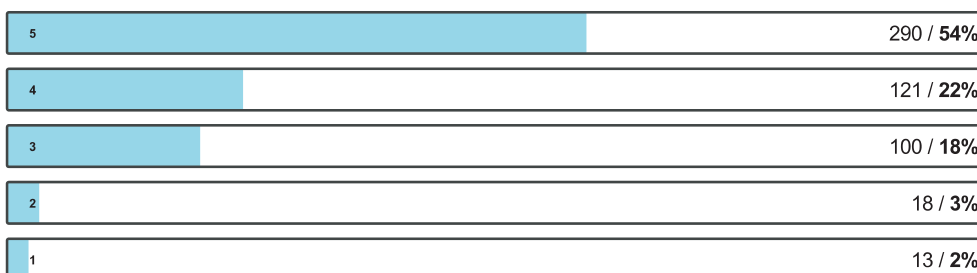


The entrusting of bookkeeping to other entity or practitioner should be regulated by law in more detail

542 of 583 answered this question

Average: 4.21

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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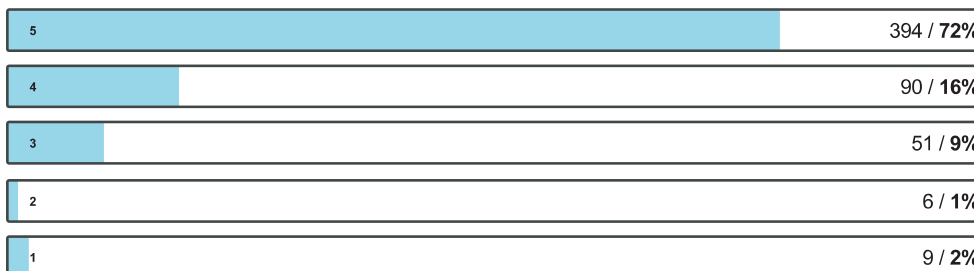


Quality financial reporting demands obligatory certification and continuous development of professional accountants

550 of 583 answered this question

Average: 4.55

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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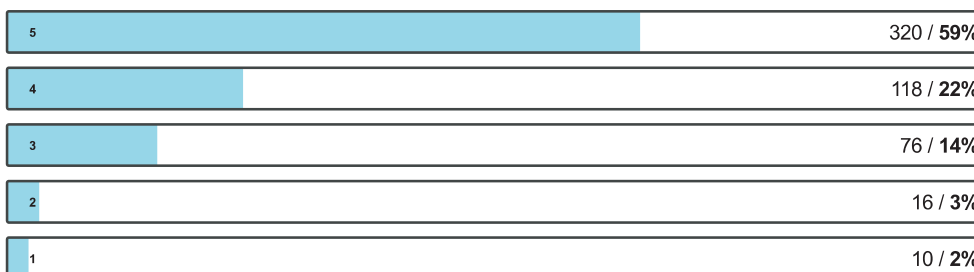


The application of IAS/IFRS increases comparability of information on national, regional and international level

540 of 583 answered this question

Average: 4.34

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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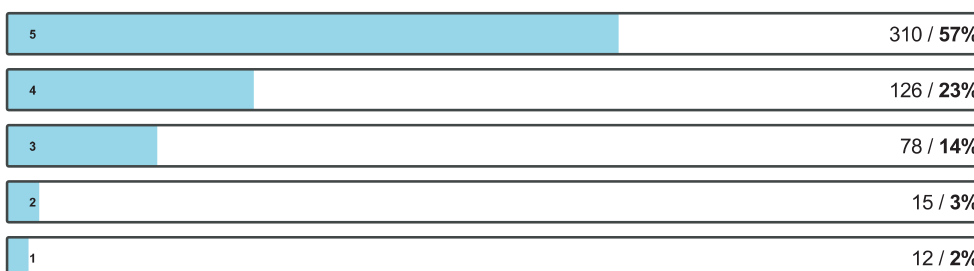


The application of IAS/IFRS increases competitiveness of the companies that want to do business on foreign markets

541 of 583 answered this question

Average: 4.31

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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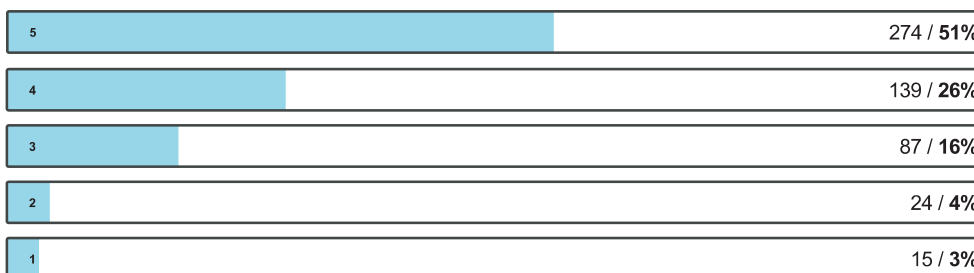


The application of IAS/IFRS helps state bodies, government agencies and companies attract foreign investments

539 of 583 answered this question

Average: 4.17

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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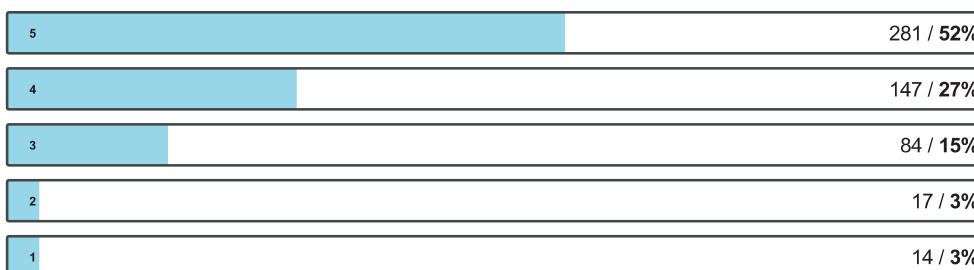


The application of IAS/IFRS and supporting regulations increases the trust of foreign investors and the quality of financial reporting

543 of 583 answered this question

Average: 4.22

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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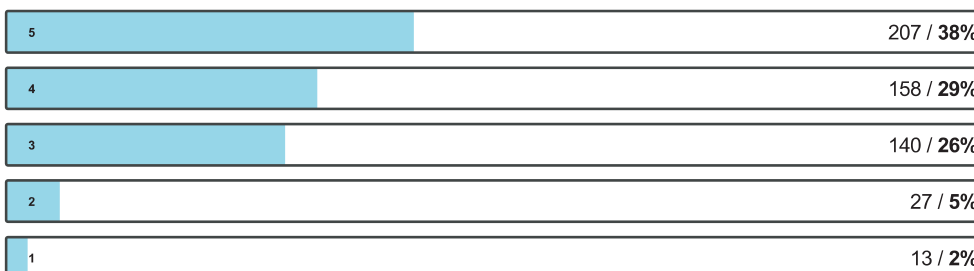


Financial statements in Serbia are not a good basis for the predicting of business events and decision-making

545 of 583 answered this question

Average: 3.95

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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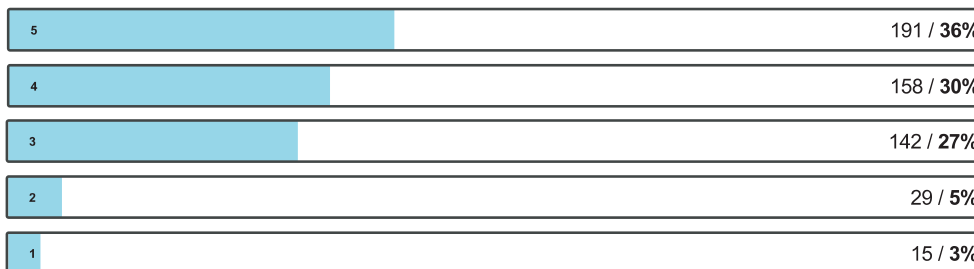


Financial statements in Serbia often contain errors, biased (not objective) information and do not always contain good descriptions needed to clarify the substance of a given item

535 of 583 answered this question

Average: 3.90

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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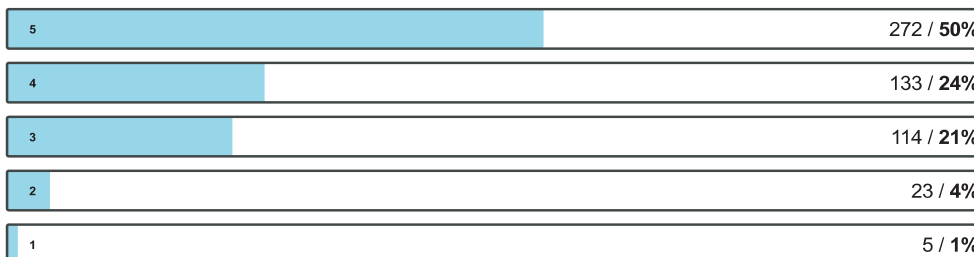


Financial statements in Serbia are not comparable (due to frequent changes and balancing inconsistencies) between different time periods, or with financial statements of other companies in the world

547 of 583 answered this question

Average: 4.18

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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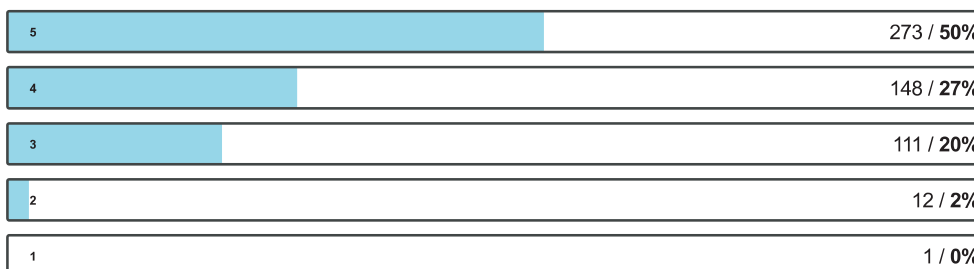


The application of different normative bases makes information more difficult to verify and hard to understand by various users

545 of 583 answered this question

Average: 4.25

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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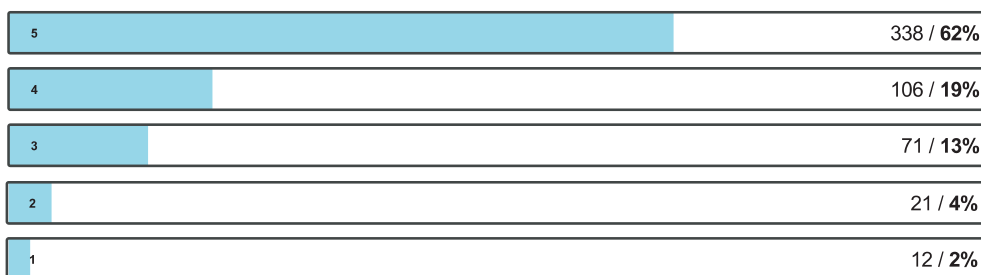


Information in financial statements are not timely, due to the requirement that financial statements be submitted up to six months as of the end of the business year

548 of 583 answered this question

Average: 4.34

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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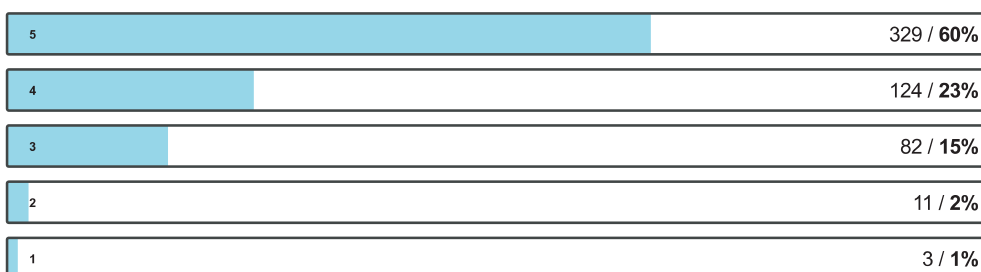


Great volume of information in financial statements (absence of clear and precise presentation) jeopardizes understandability

549 of 583 answered this question

Average: 4.39

1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
------------------------	---------------	---------------------------------	------------	---------------------

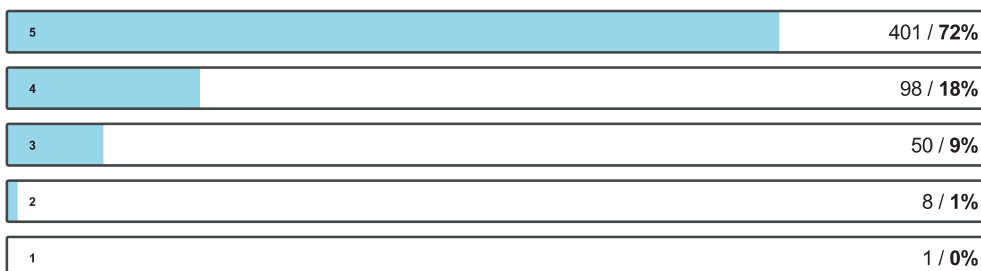


Frequent changes in the Law on Accounting (and auditing) increase the costs of financial reporting for reporting entities and all users

558 of 583 answered this question

Average: 4.59

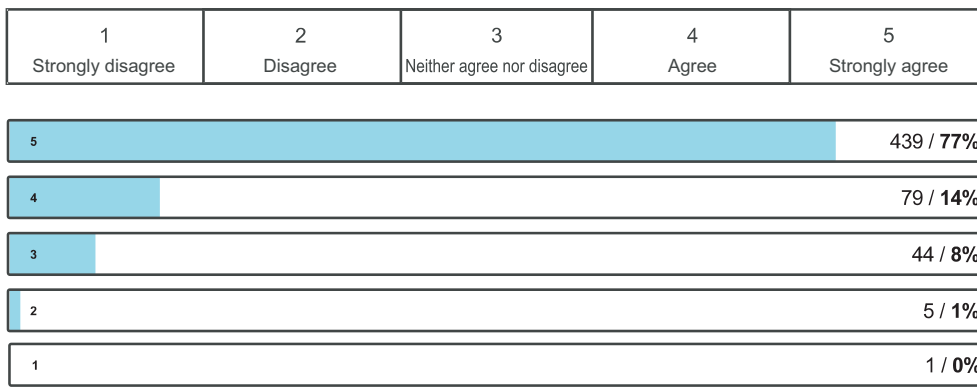
1 Strongly disagree	2 Disagree	3 Neither agree nor disagree	4 Agree	5 Strongly agree
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Poor legislative solutions have led to the deterioration of accounting and accountancy profession, and endangered public interest

568 of 583 answered this question

Average: 4.67



6. Key Attitudes of Professional Accountants

Analysis of results of the empirical research identified key positions, which on average represent 85% of the surveyed professional accountants relating the regulatory accounting framework and the quality of financial reporting in Serbia, which are listed below.

1. Poor legal solutions and lack of updated translations of IASs / IFRSs and IFRSs for SMEs and supporting regulations have led to a threat to public interest, impairment of accounting and the accounting profession and disabling quality work of accountants and auditors. Accordingly, professional accountants believe that the statutory accounting regulations should be of high quality, comprehensive, stable and without frequent changes which increase the reporting process costs (this attitude is expressed by 91.2% of the surveyed accountants).
2. The application of IASs / IFRSs, IFRSs for SMEs and other professional regulations contributes to: the comparability of financial statements, increased competitiveness of domestic companies on foreign markets as well as to the strengthening of confidence of foreign investors in financial reporting. The preparation of financial statements in accordance with this regulation undoubtedly assists the public authorities, government agencies and companies themselves, in attracting foreign investment (this attitude is expressed by 85.2% of the surveyed accountants).
3. All reporting entities, regardless of their classification by size, should be allowed to apply the 'full' IASs / IFRSs, which would reduce the workload and costs in preparing the consolidated financial statements and provide

- continuity in the case of shifting from one category of classification to another (this attitude is expressed by 84.6% of the surveyed accountants).
4. The possibility of applying a single-entry bookkeeping system should be significantly reduced, and delegation of bookkeeping to another legal entity and entrepreneur should thoroughly be regulated by law (this attitude is expressed by 84.1% of the surveyed accountants).
 5. With a view to reducing the costs of reporting and providing the reliability and understandability of financial statements the number of valuation bases for balance sheet items needs to be reduced. For micro and other legal entities a special rulebook on the valuation of balance sheet items is not required, since the content of the IFRSs for SMEs is not extensive (230 pages, of which certain entities apply only certain parts) and as such is suitable for those reporting entities. The application of a large number of different normative bases makes verifiability and comparability of information in financial statements difficult, as well as their equal understanding by all financial statement users (this attitude is expressed by 82.6% of the surveyed accountants).
 6. Number of the chart of accounts in accordance with which transactions and business events are recorded in Serbia, as well as the preparation of financial statements need to be reduced because balance sheet items for all reporting entities have the same substance and terms of recognition (this attitude is expressed by 92% of the surveyed accountants).
 7. Reducing the number of valuation bases and the number of the chart of accounts, decreases the need for separate form of financial statements for certain reporting entities (for example, other legal entities - this view is expressed by 82.6% of the surveyed accountants).
 8. Current financial statement forms are overly cumbersome, do not always include clear and concise descriptions for a full understanding of contents of certain positions, which impairs their understandability and as such, they do not serve their purpose (this attitude is expressed by 78.7% of the surveyed accountants).
 9. Financial statements in Serbia do not present a good basis for forecasting business events and decision-making because they often contain errors, do not always contain valid descriptions, are not comparable within the reporting entity due to frequent changes, or with reports of entities from other countries, because they are too cumbersome both in form and content and not harmonized with current international regulatory framework. The above indicates that due to poor quantitative and qualitative characteristics, financial statements in Serbia are not a good basis for understanding the financial position and performance of the reporting entity. In addition, information provided in the financial statements are untimely because it is published 6 months after the end of the business

year and unreliable due to the possibility of changing the financial statements submitted to the competent authority by the end of next year compared to the year for which the reports had been prepared. For these reasons, the submission of regular financial reports shall be done by the end of February of the current year for the previous year, while using the same reports for statistical purposes, and the possibility of replacing the financial statements at the discretion of reporting entities should be revoked (this attitude is expressed by 81.3% of the accountants surveyed).

10. The quality of financial statements and their reliability would increase and a better insight would be provided in the payment of bookkeeping service tax, by introducing the obligation of signing the financial statements by professional accountants, by reintroducing the Education Standards and the Code of Ethics for Professional Accountants into the legislation, as well as by the introduction of substantial responsibility of the providers of accounting services who meet the certification and continuing education requirements, all of which would bring Serbia closer to the countries with developed financial reporting practices. Improved legal and professional control of financial reports would reduce the level of risk of the mistakes contained therein, as well as the level of gray economy in Serbia (this attitude is expressed by 85.1% of the surveyed accountants).

Conclusion

Financial reporting aims to provide valuable information for the economic reasoning and decision-making of investors, creditors, government institutions, business partners, employees and labor unions, business and financial circles, regulators, rating agencies, financial analysts, investment advisers, consulting agencies, statisticians etc. It is an important and indispensable part of the financial infrastructure of any economy and the basis for the stability of every national and international financial system.

Financial reporting is a key infrastructural support for efficient and transparent functioning of the capital market, as it leads to the allocation of capital that promotes productivity, encourages innovation, provides the conditions for maintaining the liquidity of capital markets, facilitates lending, etc. Oversight function of regulatory bodies of capital markets is based on financial statements.

Economic policymakers rely on financial statements to identify structural financial problems, the level of indebtedness of economy, problems of insolvency, the burden of financial expenses, etc. They point to profitability and level of competitiveness of particular sectors, industries and enterprises.

Financial reporting is important for company management because it is necessary for them to analyze their own and other companies' financial position and performance, in order to evaluate and assess business and financial risks.

Quality a priori and transparency are the imperative of financial reporting for which the responsibility is held by the state, national regulators, professional accountancy organizations, independent bodies for public oversight, and also the management, the audit committee and professional accountants, including auditors.

The quality of financial reporting in Serbia is at a very low level because it is not compliant with European Union regulations, nor with the international professional regulations as a key criterion for that quality. For a significant number of reporting entities specific national regulations are prescribed, which lack both practical and theoretical foundations. Financial reporting in Serbia lacks stability and consistency. The ethics of professional accountants, including auditors, as the basis of modern professionalism in the regulations of the Republic of Serbia, is almost ignored. Professional accounting organization, which is a natural "guardian" of the quality of financial reporting and the protector of the public interest in developed cultures of financial reporting, which exists and operates in Serbia in accordance with the rules of the profession for more than 60 years and is a member of IFAC, is not mentioned at all in this regulation.

The structure and content of financial statements in the Republic of Serbia is unsuitable for any financial reporting practice, with relevance and reliability of the information contained in them also being impaired, and transparency is just another issue. Such financial statements are not a good basis for economic reasoning and de-

cision-making of any of their numerous users. Likewise, company management does not have a quality information base for management.

Financial reporting environment in the Republic of Serbia is based on a substantial unawareness of the importance of financial reporting and of the consequences of poor quality financial reporting, and is therefore reduced to a formal obligation to submit financial statements on a particular day, with the possibility of amendment. Legal and professional regulations are also created on such a basis, thus ignoring factual available resources of proven quality, dividing the main participants in the financial reporting process, and inaugurating wrong and dysfunctional institutions, while completely liberalizing the market of accounting services and the like.

The results of such regulation of financial reporting in the Republic of Serbia was rated as negative, in all relevant aspects, by 583 professional accountants in a highly respectable survey, organized in 16 target cities in Serbia.

Appendices

Appendix 1.
Survey Questionnaire

**SURVEY IS ORGANIZED BY SERBIAN ASSOCIATION OF ACCOUNTANTS AND AUDITORS
AND BY PROFESSORS OF THE FACULTY OF ECONOMICS**

SURVEY

**Regulatory framework of accounting
and the quality of financial reporting**

Dear Sir or Madam, you have in front of you a questionnaire the results of which should provide insight into your views related to the current situation and the improvement of accounting regulations. Please answer each question by **rounding off one of the listed numbers** (1 to 5) or letters. **The questionnaire is anonymous** and will be used as an argument for the benefits of the proposal to the legislative bodies in connection with the announced amendment of legal accounting regulations. **Thank you in advance for your cooperation!**

Employed:	a) at a company, financial institution, etc.		b) at an agency that provides accounting services	
Work experience:	a) Less than one year	b) From 1 to 5 years	c) From 6 to 10 years	d) Over 10 years
Size of company:	a) Big	b) Medium	c) Small	d) Micro
Legal form of the company:	a) Joint stock	b) Ltd.	c) Public-owned	d) Other
Sector / Industry (write)				

In completing the questionnaire, please indicate the extent to which you agree with the above statements:

Strongly agree **round off 5**

Disagree **round off 2**

Agree **round off 4**

Strongly disagree **round off 1**

Neither agree nor disagree **round off 3**

No.	Statement	Strongly agree	Agree	Neither agree nor disagree	Disagree	Strongly disagree
1.	Implementation of IFRS and IFRS for SMEs requires stable and quality professional regulations (without frequent changes).	5	4	3	2	1
2.	A high number of bases on which balance sheet items are valued, does not contribute to the reliability of reporting, while it increases costs and demands more effort from the accountant.	5	4	3	2	1
3.	The existing financial statement forms, because they are too big and contain errors, do not serve their purpose.	5	4	3	2	1
4.	If the scope of financial statements is decreased, there would no longer be need for special forms of financial statements for particular reporting entities.	5	4	3	2	1
5.	All entities, regardless of their classification, should be allowed to apply full IFRS, which would result in the decrease of the amount of work, number of mistakes, and costs of transmission from one category of classification to another, as well as with consolidation.	5	4	3	2	1
6.	The lack of updated translations of IFRS, IFRS for SMEs and supporting regulations hinders the quality work of accountants and auditors.	5	4	3	2	1
7.	Single entry bookkeeping should be regulated in more detail and reduce this possibility to the entrepreneurs with no more than two employees and with modest turnover.	5	4	3	2	1

8.	The rulebook for the valuation of items for micro and other entities does not provide all the necessary information for the recording of operational changes, without the usage of IFRS for SMEs.	5	4	3	2	1
9.	Since the IFRS for SMEs is in use, there is no need for the special rulebook for micro and other entities.	5	4	3	2	1
10.	Other entities should not be separated either by financial statement forms or by chart of accounts.	5	4	3	2	1
11.	The existence of 13 charts of accounts makes it more difficult for the accountant to do his or her job, because the balance sheet positions in all entities have the same essence and terms of recognition.	5	4	3	2	1
12.	Regular financial statements should be submitted on February 28 (29), and they would be used for statistical purposes.	5	4	3	2	1
13.	The possibility of replacing financial statements should be abolished.	5	4	3	2	1
14.	The signing of financial statements by certified professional accountants who possess the required knowledge and skills, would restore faith in the quality of financial statements.	5	4	3	2	1
15.	The return of education standards and Code of Ethics for professional accountants in legislation would contribute to the reliability of financial reporting.	5	4	3	2	1
16.	The control of financial statements is at a very low level, which contributes to gray economy and corruption.	5	4	3	2	1
17.	By introducing the accountability of the providers of accounting services, the state would have an insight into tax collecting on that grounds.	5	4	3	2	1
18.	The entrusting of bookkeeping to other entity or practitioner should be regulated by law in more detail.	5	4	3	2	1
19.	Quality financial reporting demands obligatory certification and continuous development of professional accountants.	5	4	3	2	1
20.	The application of IAS/IFRS increases comparability of information on national, regional and international level.	5	4	3	2	1
21.	The application of IAS/IFRS increases competitiveness of the companies that want to do business on foreign markets.	5	4	3	2	1
22.	The application of IAS/IFRS helps state bodies, government agencies and companies attract foreign investments.	5	4	3	2	1
23.	The application of IAS/IFRS and supporting regulations increases the trust of foreign investors and the quality of financial reporting.	5	4	3	2	1
24.	Financial statements in Serbia are not a good basis for the predicting of business events and decision-making.	5	4	3	2	1
25.	Financial statements in Serbia often contain errors, biased (not objective) information and do not always contain good descriptions needed to clarify the substance of a given item.	5	4	3	2	1
26.	Financial statements in Serbia are not comparable (due to frequent changes and balancing inconsistencies) between different time periods, or with financial statements of other companies in the world.	5	4	3	2	1
27.	The application of different normative bases makes information more difficult to verify and hard to understand by various users.	5	4	3	2	1
28.	Information in financial statements are not timely, due to the requirement that financial statements be submitted up to six months as of the end of the business year.	5	4	3	2	1
29.	Great volume of information in financial statements (absence of clear and precise presentation) jeopardizes understandability.	5	4	3	2	1
30.	Frequent changes in the Law on Accounting (and auditing) increase the costs of financial reporting for reporting entities and all users.	5	4	3	2	1
31.	Poor legislative solutions have led to the deterioration of accounting and accountancy profession, and endangered public interest.	5	4	3	2	1

Appendix 2.
List of cities where the survey was conducted

The survey was conducted in the period from 16 to 30 June, 2016, in 16 cities in Serbia:

- Subotica
- Nis
- Pozarevac
- Pirot
- Sremska Mitrovica
- Vrsac
- Novi Sad
- Sombor
- Kragujevac
- Pancevo
- Backa Palanka
- Zrenjanin
- Novi Sad
- Belgrade
- Krusevac
- Kikinda

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