

# Chapter 6

## Policy Options Proposal

March 2016

**This chapter should be cited as**

ERIA (2017), 'Policy Options Proposal', in Mizunoura, K. (ed.), *Accounting Standards for Small-and Medium-Sized Enterprises in ASEAN*. ERIA Research Project Report 2015-22, Jakarta: ERIA, pp.157-178.

## Chapter 6

### Policy Options Proposal

Needless to say, bookkeeping and accounting play critical roles in ensuring healthier operations and consistent growth of SMEs. In particular, for the coming ASEAN integration and increasing globalisation, economies should justify keeping books and accurate financial statements, even by SMEs, as not only absolutely imperative for their expanded business transactions and global evolutions but also critical for maximising access to finance, which a growing issue in these nations.

In contrast, our research has revealed that there are some variances in entity size among nations; that not a few of them do not even document financial statements; and that if they do, the statement records are given less credibility by banks or accountants. Some even referred to the limited number of SMEs with diligent bookkeeping, even for daily transactions. There is a wide gap between the ideals and the reality of the system, and this gap must be resolved.

As symbolised by the economic integration of ASEAN countries in 2015, the globalisation of the economy and business is unavoidable. Unless this trend is understood without fail, the ASEAN countries will not be able to achieve further economic development.

From the viewpoint of accounting, the adoption of IFRS and IFRS for SMEs would be ideal, leading to conformity with the trend of globalisation. However, various challenges exist such as: companies are not conscious of the adoption of IFRS for SMEs; and it is difficult to implement IFRS due to lack of resources, et cetera.

In this section, we will explain in detail what our research has revealed, as well as the desirable policies we have heard from SMEs, economy-related authorities, tax authorities, financial institutions, and accounting professionals, and we will summarise recommendations on policies to be implemented in ASEAN.

### **Potential Inhibitors for Bookkeeping and Financial Statements Documenting in SMEs**

Our research has determined that potential inhibitors keeping SMEs from accommodating bookkeeping and financial statements can be classified into three major aspects.

The first inhibitor is the mindset of SME owners in that they are not motivated to keep books and financial statements at all. These owners do not understand the advantages of bookkeeping and documenting financial statements of their businesses, and some even go as far as dual bookkeeping. Some of them also think the disadvantages outweigh the advantages because bookkeeping can lead to higher chargeable taxes. Changing their mindset towards bookkeeping and financial statements should be the first task.

The unavailability of resources to SMEs is the second inhibitor. Even with better mindset towards bookkeeping and documenting financial statements, SMEs have no other choice but to hire internal specialists or outsource the service, which is an additional cost factor. Also, even personnel with higher expertise such as accounting majors from universities wind up less qualified because they often have a hard time understanding the rapidly changing accounting standards or accounting rules. To make it worse, the cost of hiring these 'less qualified' talents is increasingly high, thanks to their limited population. It is therefore essential to provide a certain level of support to address these challenges as a government initiative to assist SMEs.

Associated with lack of resources, the third inhibitor is the excessively advanced and complex structure of the accounting standard and the rules that SMEs have to accommodate, versus resource and business objectives. Though it sounds reasonable to say that even SMEs should adopt the advanced and complex standard, provided they foresee larger scale and increased international transactions in the future, it will not make a solid sense to suddenly make them accommodate such rules that the big boys in advanced nations implement because SMEs have no experience in bookkeeping or documenting financial statements. So that SMEs can initiate the effort of diligently managing accounting, it will be critical to lower the barriers by putting in place an accounting standard that will allow easier adoption or development and information delivery of guidelines.

The section below summarises the possible government initiatives that will overcome these inhibitors.

## 1. Initiative to better motivate SME owners

For more active involvement by SMEs in accounting, owners of SMEs have to start by executing lead-by-example type of leadership to accommodate the accounting standard. However, responses to our research have revealed that SMEs are keeping books out of necessity for tax payment, or are submitting books and financial statements out of necessity because it is compulsory. Furthermore, there were respondents who emphasised the disadvantages. Some comments were: 'I would rather refrain from submitting them out of fear of getting higher tax charged' or 'out of potential of undesired leak of our financial status to competitors'. All these taken into account, the utmost challenge seems to be how to better motivate SME owners to implement diligent accounting practices.

Three key measures to better motivate them are recommended below:

The first set of measures is to recognise the significance of putting diligent accounting into practice to help them understand how this can be leveraged for their business management.

The second set is to make the incentives for putting diligent accounting into practice clearly visible. Once the logic that conducting diligent accounting can lead to direct/indirect monetary benefit is understood, chances are that SME owners may be more motivated and gain a better weapon to allow improved accountability and directions over shareholders and employees.

The last one is clear visualisation of the disadvantages of non-conformance to the accounting standard. Though motivating someone to be involved through providing disincentives is not always ideal, usually, such disincentive initiative for a limited period may effectively work. Our research found comments such as: 'No one would be motivated until they clearly understand that the conformance is a duty' or 'I see no penalties for not keeping (books)'.

The sections that follow give detailed views of directions and specific conceptual pictures of these three sets of measures.

### (1) Recognising the significance of diligent accounting

~'If you understand accounting, you can look over the business.'~

One of the reasons that bookkeeping and documenting financial statements are not gathering much attention from SME owners seems to be that not a few of them accept the resulting cost as it is forced, or it is just a boat anchor. In this regard, they need to properly recognise

that diligent accounting is something that will enable the growth of an enterprise through solid management of accounting. It is important to make them deepen their understanding that if they understand accounting, they can look over the business.

#### 1) Promoting the of understanding of the fundamental significance of accounting

It is necessary to proactively communicate to SME owners that diligent accounting enables effective and efficient business management, and that it can be an effective leverage for savings against future investments, allocation of revenues into right records, prevention of bankruptcy by secured loan repayments, as well as development of effective strategies based on accurate understanding of operating results.

**Specific options** for this initiative may include accommodating accounting into government-held training programs on business management for SME owners, rolling out an educational campaign collaborated by government bodies and CPAs, or even informative activities for communities or workshops organised by SME owners at their will.

#### 2) Presenting specific success cases of better operating results, thanks to proper utilisation of accounting

There is nothing wrong about SME owners focusing on growing revenues and profits in a tough market environment. Accordingly, the sharing of successful business scenarios attributable to fully utilised diligent accounting would be a powerful incentive for SME owners to take accounting efforts seriously.

Letting them know that making full use of diligent accounting has enabled business size expansion and better profit and loss statements will make them more involved. Moreover, providing detailed case analysis, including which components of accounting were used at what time, would allow them to replace the success case with their own and consider what to do.

**Specific options** for this initiative may include efforts by leadership of government bodies or the like to collect and publish domestic and overseas successful scenarios of proper accounting. Serious effort has to be made at detailed and specific analysis of those scenarios and rearranging them into something that would motivate the SMEs to use accounting.

Below are extracts of successful cases from a success case compilation in Japan, which may be used to create an image of concrete measures.

**Table 42: Cases of companies that obtained results from the adoption of accounting standards (Cases in Japan)**

Result obtained	Description of the case
Cost reduction	Numerical data obtained through accounting processing started to be disclosed at meetings attended by employees. As a result, all the employees became able to examine sales strategies, et cetera from the same viewpoint. At first, many employees were ignorant of accounting. But they began to understand accounting gradually and became more cost conscious, which led to cost reduction. (Toho Auto Mobile Co., Ltd./automobile/ 78 employees)
Revenue growth	The management became better at financial analysis, thanks to the introduction of the accounting standard, the accounting software, and the guidance of tax accountants. As a result, they started to analyse the information and succeeded in shifting from low value-added processing to high value-added processing. They could obtain more than 20 clients during two terms. (Imahashi Co., Ltd./ metal machining/13 employees)
Increased confidence from financial institutions	As a result of the introduction of the accounting standard, monthly inventory clearance, which had been a constant problem, was put into practice. When the company asked for a loan, the financial institution demanded provision of the monthly trial balance, which could be immediately produced. The company gained the confidence of the financial institution, so not only did they obtain a loan, but they also obtained a low interest rate. (Yoshio Co., Ltd./ manufacture and sale of machinery/7 employees)

Note: The cases above are presented in more detail in the original case book, but they are summarised here to be used as examples.

Source: 65 Selected Cases of Companies Tackling the Standard for Small and Medium Enterprise, SMEA, March 2014.

### 3) Extending recognition for enhanced 'Access to Finance'

Enhancing SME access to finance is one of the challenges within ASEAN. This initiative may include a bridging finance until a promising SME start-up realises stable income; financing a successful SME for extended investments; or helping an SME in tentative working capital shortage under various circumstances with cash financing. Enhancing access of SMEs without scalable start-up capital to finance goes beyond just helping that particular SME and can lead to mid- to long-term expansion of their business accounts base as well as the country's economic development. Thus, it is crucial to ensure that SMEs conducting excellent businesses are appropriately appreciated for right finance.

Multiple measures have to be taken to resolve these situations. The biggest reason for poor access to finance by SMEs is the inability of financial institutions to conduct a thorough examination of the SME's earnings and repayment capacities, making them hesitant to lend a financial helping hand. For financial institutions to properly examine these SME capacities, streamlined books and financial statement credibility play a key role.

While some SMEs are properly preparing accounting books and improving financial statements, financial institutions, including banks, do not rely on their books and financial statements because internal control is not operating properly. They insist on checking receipts and invoices of SMEs one by one. SMEs are required not only to improve their accounting books and financial statements but also to improve the quality of their internal control so as to prepare reliable books and financial statements. To prepare reliable books and financial statements, it is desirable for SMEs to adopt simple accounting standards that are not too complex but are focused on correct bookkeeping.

While this is not included in the scope of this paper, governments and central banks should take measures in partnership with public financial institutions. They should, for example, positively offer loans by giving full weight to the evaluation of books and financial institutions of SMEs, or support various efforts by private banks.

In addition to streamlining books and financial statements, the business itself has to be successful and promising. More importantly, SME owners have to be made clearly aware that better managed books and financial statements would allow better financing under more favourable terms and conditions.

As revealed by our field research, some SME owners can avail of financing by using their personal or family asset or from non-banks (including illegal ones) without having their books and financial statements examined. It is therefore obvious that resolving this issue relies on the government's efforts for streamlining the finance market.

**Specific measures** for this initiative include communicating the necessity of having credible financial statements ready for better access to finance as well as other measures that will facilitate financial support for SMEs from financial institutions by absorbing the risked money by the government, provided that the corresponding SMEs have securely streamlined the statements.

## (2) Providing SMEs with incentives

Regular SME owners living in an intensive competitive environment give their first priority to day-to-day revenues and profits even though they understand the importance of accounting. In this context, providing positive incentives for business management to use appropriate accounting and have bookkeeping streamlined is necessary. A few options for this initiative

are discussed below.

#### 1) Incentive granting

Though a variety of options for granting incentives for enterprises with organised management and books and financial statements in place are available, the most comprehensive option with solid acceptance in non-ASEAN nations involves the granting of preferential interest rates and taxation.

With the **preferential interest rates policy**, debtors are entitled to favourable interest rates for finance by banks on the condition that their financial statements conform to a given accounting standard. This is a powerful incentive for SMEs and has been established as a regular policy in Japan and some other countries. The creditor banks determine the interest rate by not only checking the availability of diligent and standard financial statements but also by examining the profitability and stability of the debtor's business. **Specifically**, the government and the banks will have to generate the fund for this policy by sharing the opportunity loss by the interest rate difference.

With **preferential taxation**, enterprises with diligently kept books and financial statements are entitled to a lower corporate income tax amount. Measures with established acceptance (such as the Blue Return System which is also available in Japan and other countries) can be used as a reference. Though the short-term tax revenue declines due to the lowered tax rate, the government can expect increased mid- to long-term tax revenues as long as the SMEs realise higher income and profits out of the expanded business attributable to better business management with proper use of accounting. **More specifically**, this option requires collaborated efforts by the government agencies in charge of SMEs and those in charge of internal revenue.

As explained in the case of the Blue Return System in Japan, it would be helpful to introduce a system where SMEs can receive tax benefits or their accounting books are granted credibility against inquiries by the tax authorities if they properly keep accounts and prepare financial statements in accordance with an appropriate bookkeeping principle. In addition, it should be noted that documents for tax return and closing financial statements under the commercial/corporation law can be simultaneously completed, thanks to the adoption of the 'definite settlement of accounts' principle in Japan. This gives SMEs great incentive in that even small companies with little resource, knowledge or experience concerning accounting



and tax affairs can complete the procedures with a relatively small effort.

It is important to note that such incentive measures are achieved through the coexistence of a system for encouraging appropriate bookkeeping (such as the Blue Return System) and the 'definite settlement of accounts' principle. Care should be taken to ensure such coexistence if adoption of incentive measures as mentioned above is to be considered.

Though direct opportunities for SMEs' increased income or profit cannot be expected, unlike the preferential interest rates and taxation options, another option is to qualify bidders and contractors for government procurement tenders if their financial statements conform to a given accounting standard

## 2) Eliminating disincentive factors

This research has also identified that legacy systems or practices, which potentially work as disincentives against proactive keeping and usage of books and financial statements by SMEs, still exist in some countries. For example, Cambodia adopts an estimated taxation system (Estimated Regimes) in which tax rates are determined according to the government-defined business lines and categories, mostly because sole proprietors in the country do not properly keep books, making it difficult to calculate accurate taxable income. Our hearings have also revealed that a calculated tax amount is generally less with Estimated Regimes than with taxation based on actual business revenues, which often result in cash losses by properly keeping books.

The Cambodia example is illustrative only but other cases where bookkeeping and documenting financial statements work unfavourably for businesses exist. Initiatives that eliminate these disincentive factors and enhance the motivation of SME owners for accounting should be implemented.

## (3) Enforcing policies (with visible and effective penalties)

### 1) Definitive enforcement of documentation and submission of financial statements

Bookkeeping and documenting financial statements are supposed to be pursued proactively by enterprises at their will. However, as responses to our field research has revealed, 'the most important for SMEs is to do what is compulsory' and 'it is not clearly defined if documenting financial statements conforming to accounting standards is mandatory'. It is true that clearly defined enforcement or outstanding penalties in place will allow easier focus

on accounting.

**One specific option** to address these challenges is to clearly communicate the enforcement of bookkeeping and documentation, and the submission of financial statements. As suggested in a response to our field research, it could be a feasible option to draft a law such as the 'Financial Statements Act', which provides clear-cut definition of the duties of business entities.

## 2) Screening of financial statements by government bodies or the like

Unless submitted financial statements are examined for its appropriateness versus the given accounting standard or, for credibility, just making bookkeeping and documentation and submission of the statements a mandatory duty of an enterprise will not lead to a diligent attitude towards documentation. The examination has to go beyond just checking and submission. It has to be a detailed examination of the records.

**One specific option** to address this challenge is to implement due diligence by the government body receiving the books and financial statements from SMEs. As this is already in place to a given extent in Thailand, their framework and practices should be a reference model. Though examining all submitted statements is a distant idea, even a sample investigation shall effectively work as check and balance against SMEs. Additional effects can also be expected by calling for repetitive corrections or by imposing penalties when some defects are identified after actual screening.

Moreover, obligating a simplified audit by accounting specialists can be an alternative if the examination of financial statements by government bodies is not realistic, though the level of audit may hardly match that of large corporations or publicly-traded firms. However, it should be kept in mind that some allowance might be necessary to compensate for the cost of audit as documenting financial statements already has a negative impact on the overall cost burden on SMEs.

## 3) Tightening control over dual bookkeeping

Though clearly different from the other issues, some respondents (financial institutions and CPAs) pointed out that the books and financial statements are not credible because not a few SMEs use dual bookkeeping. Unless the government body in charge undertakes a serious action to control this, it will take forever to realise accurate, highly objective, and credible

books and financial statements, which also keep these SMEs which using double bookkeeping from being accountable for examinations, including for financing.

A **specific option** to resolve this issue is to tighten control over these ill behaviours, including dual bookkeeping. As the representative purpose of dual bookkeeping is either tax breaking or reduction, collaboration with the government agency in charge of taxation will be critical.

## **2. Initiative to compensate for lack of resource for accounting in SMEs**

In the implementation of the aforementioned policies and options, a potential inhibitor for SME owners' efforts on diligent accounting—after recognising the materiality and advantages of keeping books and financial statements in place (or the disadvantages of not doing so)—is the lack of resource. The resources mentioned here are specifically monetary and personnel resources.

SMEs conducting businesses under intensively competitive environments are often not blessed with excess funds and not a few of them lack monetary resource to implement diligent accounting. Even if some of them are blessed with that resource, the other challenge they face is the internal or external availability of appropriate personnel who will implement the expected diligent accounting. A comment from our field research also pointed out that while hiring a specialist who studied accounting in a university costs more than a regular staff, his/her skill level may end up being lower quality because the specialist cannot respond to the rapidly changing accounting environment. Another comment pointed out that the population of highly skilled experts—such as CPAs who have updated knowledge of new international accounting standards and the talent to instruct other staff— is limited in local areas.

SMEs owners need to have a positive mindset for implementing diligent accounting and supporting talented personnel to make it as an operational practice without substantial additional cost.

### **(1) Addressing lack of monetary resource (including financial assistance for employment)**

Achieving growth in revenues and profits is the utmost goal of SMEs and, with limited capacity to respond to requirements, including legal ones, accounting is not necessarily a high priority among SME owners (in the context of priority-based and leveraged use of available

funds), even if the owners solidly recognise the importance of accounting. Thus, gaining monetary resource, which can be allocated solely for accounting, will lead to a resolution of this challenge.

**A specific and most comprehensive option** to resolve this issue is to make subsidies available to SMEs with advanced accounting by a government body or other public institutions. In case the government body alone does not have sufficient budget, collaborative interaction to build the funds with entities such as CPAs and banks should not be impossible.

Moreover, if the government is projecting deeper involvement in SME support, combining the 'successful scenarios propagation' strategy with the provision of subsidies for accounting enhancement and improvement of qualified SMEs (after publicly calling for applications for those with promising businesses) can be another option. By making successful applicants committed to publishing the post-subsidies results in the 'successful scenarios', the government can also benefit.

## (2) Addressing lack of personnel

After SME owners decide to initiate diligent accounting efforts, they will face the next challenge: the person who will carry out diligent accounting cannot be found internally and externally. As not a few countries go through dramatic and frequent accounting system changes, personnel with solid knowledge of diligent accounting and ability to implement are not always available and require higher compensation than regular employees to hire. The other issues are: there are often no external candidates or experts with high quality to outsource the accounting operations; or the cost of hiring the service is extremely high. The following measures can be implemented to resolve these issues.

For example, the establishment of a qualification called 'Corporate Accounting Coordinator' is being considered in Japan right now. Only those who have passed the accounting examination (such as the Official Business Skill Test in Bookkeeping 2<sup>nd</sup> Grade), can apply, and the test subjects are expected to include SME accounting, management finance, tax laws, and internal control. This qualification is characteristic in that the qualifying test is designed for human resources who are familiar with or have knowledge of tax laws, internal control, financial management, and accounting so that they can give appropriate advice to management from a finance and accounting viewpoint.

### 1) Resolving lack of accounting experts

Growing to a given scale, SMEs will hire clerical and sales staff, which will result in increased employee headcount with a variety of responsibilities. Some SMEs even hire staff that will be responsible for accounting. And because of the demand for a certain level of accounting expertise, hiring graduates from universities who majored in accounting is not a rare case. However, it was pointed out during the survey that SMEs still face issues such as inability to respond to the latest rules because the knowledge of accounting of these graduates is limited to what they have learnt in university or they have no experience in actual business operations. Also, concerns that hiring accounting personnel substantially increases the cost and that not a few accounting employees quit after acquiring accounting skills were also raised. Even so, SMEs are having a tough time finding right candidates as the availability of such accounting experts in the market remains low.

**Two specific measures** to resolve this issue have to be implemented. These are: to 'enlarge the population of human resources who study accounting at higher education, including universities' and to 'increase the number of educational institutes and programs to provide education in accounting'.

In terms of expanding the population of human resources who study accounting at higher education, including universities, more students can be expected to enrol by implementing policies that suggest that studying accounting secures better jobs or achieves higher social status. However, as secured jobs depend on active employment of accounting personnel by SMES, facilitating such employment has to be conducted in parallel with awaking the interest in studying accounting.

In terms of increasing the number of educational institutes and programs that provide accounting education, supportive measures by government bodies to increase these institutes and programs or, as a part of the SME development policy, provision by the government bodies themselves of opportunities, including accounting training programs as well as information services, can be considered. During our survey in Indonesia, some respondents pointed out that these programs are mostly standalone programs provided by different government agencies though they are already in place nationwide. To resolve this issue, it would be ideal to provide highly sequential curricula that allow step-by-step learning through, for example, inter-agency collaboration.

Another relevant challenge is keeping the tuition low to invite more students to study, even if educational institutes and programs for accounting are already available. As our field research in Cambodia revealed, because the tuition was kept low to widen opportunities for admission and enable students to learn in universities offering accounting courses, it became hard to hire quality teachers. Therefore, in addition to increasing educational institutes and programs, there must be some financial aids to allow tuitions for these institutes and programs to be kept at a reasonable range.

As observed so far, enabling an increase in the quantity and quality of students learning accounting and employees responsible for accounting by providing increased opportunities and institutes for reasonable accounting as well as promoting awareness of students on accounting will contribute to building a foundation to support SMEs tackling the accounting issues.

## 2) Resolving lack of accounting support personnel

Another challenge that SME owners will face once they initiate diligent accounting is the lack of external accounting and accounting support personnel. Our field research in ASEAN nations confirmed that some SMEs are not blessed with the capacity to hire employees only for accounting tasks and that these specialists are made responsible not only for documenting and auditing financial statements but also for bookkeeping. Though there should be a growing number of outsourced firms for accounting services as the economy develops, it is necessary to find more consulting firms with high quality providing services at reasonable fee schedules that SMEs can afford in order to support those that are motivated to implement diligent accounting.

The other responses pointed out that the population of CPAs providing consultations and audits or the professionals involved in accounting should not be necessarily small, both quality wise and quantity wise, except in local areas. A certain number of experts need to be secured as the economy develops. Since CPA is a tough certificate to obtain, another effective option to enlarge the pool of accounting support personnel would be to adopt a qualification system to certify possession of adequate level of accounting knowledge and skills if not compatible with CPAs.

Moreover, it is desirable to have assessment institutes with specific expertise ready for the fair asset measurement, as an example, after introduction of IFRS or IFRS for SMEs. The

institutes that provide advanced support around accounting are also part of the 'accounting support personnel' in a broader sense and the development of these institutes or their enticement from other countries should be also required in the future.

### **3. Enabling easier implementation of diligent accounting**

In the mid to long term, as long as SME owners are highly motivated to tackle accounting issues; adequate incentives to support this motivation are provided; and supply of accounting support personnel is ensured, SMEs will be able to work diligently on accounting.

However, if the accounting standard is beyond what is appropriate for SMEs or requires greater care and cost than reasonable, SMEs might have to respond to the accounting need well beyond the original purpose of 'leveraging accounting for business management', which will cast a shadow of concern over the propagation of accounting as a good tool for use at its full value.

There are SMEs aspiring for IPO, overseas trading, global expansion, and mergers and acquisitions with overseas corporations. There are also SMEs aiming for local expansion by multi-store operation, ready to become the local number one, or even working on the development of the world's first technology. Therefore, different accounting standards should help SMEs with different corporate goals.

Meanwhile, IFRS or IFRS for SMEs is getting adopted in ASEAN nations in accord with the global trend around accounting. However, the status of responding to and positioning of the IFRS introduction is different for different countries. During our research, the following observations were made: 'The accounting standard of SMEs is not adequately respected when it comes to its actual usage.' or 'The standard is extremely a big burden on SMEs', even in a country that already completed its introduction a few years ago. Even in countries that have decided to introduce it and are getting ready for implementation in a few years, some voiced the following opinions: 'There is concern about the capacity to respond to the implementation as

increased accounting-related work is anticipated’ or ‘After all, compliance with the new standard might not be achieved.’

For SMEs lacking monetary/personnel resources and with inadequate interest in or understanding of accounting standards, the difficulty in responding to the standard or the workload in itself has become a barrier for diligent use of accounting. In fact, in Cambodia, which has already introduced IFRS, our research has identified a scenario to review the feasibility of first implementing a simplified accounting format for SMEs to realise mid- to long-term propagation and conformance.

Rather than calling for conformance by immediately setting high hurdles, an outstandingly critical option is to put in line a simplified accounting standard and a documenting guideline for small- and micro-sized entities so they can execute and get a sense of diligent accounting approach and significance.

#### (1) Introducing a simplified accounting standard appropriate for SMEs

##### 1) Simple accounting standard as a step towards compliance with international accounting standards

In the Philippines, where IFRS has long been in place and IFRS for SMEs has just recently been introduced, one response to our research pointed out that the standard is too cumbersome for SMEs to respond to and imposes substantial burden on them. There are concerns about the overriding expectations before actual introduction in Thailand and Malaysia, which have made a decision to implement IFRS in the future. Another response pointed out that the standard has no value to SMEs unless they are aspiring for IPO. There were also significant objections from SMEs who are concerned that the workload would be extremely heavy.

On the other hand, there was a comment pointing out that it is not appropriate to be an only country that will not respond to international accounting standards based on global competitiveness perspective as ASEAN economic integration towards 2015 is just around the corner. SMEs should not turn their eyes away from these international accounting standards simply because they are SMEs.



Combining these environmental circumstances, it may make more sense to start by implementing a simplified accounting standard as a remedy at hand so that SMEs with no experience in keeping books and financial statements or with no accounting knowledge and skills can move forward to leveraged use of accounting with future use of IFRS or IFRS for SMEs considered. However, an excessively ‘simplified’ standard like a bookkeeping format with only brief receipt and payment entries will diminish the concept of "leveraged use of accounting for business management’. Thus, care must be taken to avoid SMEs' misperception that no advantage is found in diligent accounting.

**Figure 43: Staged development of accounting requirements for SMEs (conceptual)**

<b>Standards</b>	<b>Scope of Disclosure Audience</b>	<b>Resource for Accounting</b>
<b>(future goals)</b> <b>International Accounting</b> <b>Standards: IFRS, IFRS for SMEs</b>	Large (foreign investors, business accounts, banks, regular shareholders, analysts, tax authorities)	Sufficient accounting headcount with outsourcees or consultants externally available
↑		
<b>(Accounting required today)</b> <b>A simplified standard with SME focus</b>	Limited (business accounts, banks, family shareholders, tax authorities)	Family businesses or small/micro companies. Cannot afford external consultations.
↑		
<b>(Basic accounting)</b> <b>Formats for assisted bookkeeping</b>	None (Disclosure is not the purpose for documenting.)	Private businesses, et cetera. No affordable personnel/monetary resource.

IFRS = International Financial Reporting Standards; SMEs= Small- and Medium-Sized Entities.

2) Accounting standard which is beneficial and easy-to-use for SMEs

What kind of accounting standard then is convenient for SMEs?

Which is the most important reason for the preparation of accounting books and financial statements for SMEs? According to the field survey, the most frequently cited reasons are: 'because we have to attend tax affairs' and 'because it is obligatory under the law'. However, as explained in connection with the case of Japan, internal control does not work properly in most SMEs. We believe that emphasis should be put on accounting books (input), which are a starting point of accounting activities. It is very important for the development of companies to keep accounts on a daily basis according to rules and in a manner that ensures credibility, and to recognise and measure business on the basis of the accounting books. Emphasis should be also put on financial statements (output). They are especially important for medium to large enterprises that have many outside stakeholders or whose financial statements are evaluated in connection with mergers and acquisitions. Therefore, if the development of individual companies, in addition to the economic development, is considered, accounting standards focused on accounting books (input) are more appropriate for SMEs in the ASEAN region, whose future development is desired.

Next, it is important to ask whether the cost accounting system or the fair-value accounting (market-value accounting) system should be adopted. The framework mentioned in the discussion above will apply to this question too. For SMEs in the ASEAN region, which are expected to grow in future, the cost accounting system (which demands performance of fiduciary duties) is more appropriate than the fair-value accounting (which offers information beneficial for decision making on investment, et cetera, outside the company). The countries subjected to this research responded that the fair-value (market-value) accounting system is not enough. They pointed out that small accounting firms and local (small) audit corporations do not have the skills to respond to the fair-value evaluation, or that no business supporting evaluation of fair value (such as services for supporting market-value evaluation of assets including real estate) is sufficiently matured.

Lastly, accounting and tax affairs should be integrated rather than separated from the viewpoint of advantages to SMEs. As revealed by our field research in some ASEAN countries, the interest of SMEs in books and financial statements is mainly related to tax affairs. For example, as a result of the adoption of the 'definite settlement of

accounts' principle in Japan, SMEs, with little expertise or resource concerning accounting, can obtain benefits of increased efficiency and cost reduction because they can prepare closing financial statements under the commercial/corporation law by preparing tax declaration forms. On the other hand, SMEs can receive benefits in connection with the tax amount or prevent inappropriate taxation by the tax authorities if they properly keep accounts in accordance with a certain rule, including the Blue Return System. This may also lead to improvements in the government's ability to collect tax in countries where not only SMEs but also public functions related to tax affairs are underdeveloped.

One reference model of such accounting standards appropriate for SMEs is Japan's General Accounting Standard for SMEs. One committee member participating in our research Working Group has commented that this General Accounting Standard for SMEs, for example, should be used to establish a simplified accounting standard for SMEs in the ASEAN region, especially for small and micro enterprises that have never properly kept accounts.

If an original corporate accounting standard for small and micro enterprises is established by the whole ASEAN region, and companies that obtain an insight or experience in bookkeeping and accounting systems while they are still micro or small enterprises become matured enough to adopt an international accounting standard such as IFRS and IFRS for SMEs, this accounting system will serve as their foundation on when to seek to list stocks or expand their business across boundaries.

## (2) Communication of other information to help establish diligent accounting

It is crucial to design the accounting standard as a simplistic yet helpful tool for SME business management. Equally crucial is an initiative to deliver useful information to make the efforts of SMEs easier while eliminating the negative impression that the accounting standard is hard to understand. As specific options, providing information on accounting standards, accounting guidelines as well as software accounting applications would be effective.

For instance, not a few SME owners do not even know that different accounting

standards exist, and they cannot identify the most advantageous one for achieving their future business objectives and goals. Thus, it is crucial to communicate information on accounting in a comprehensive manner.

Also, the reality is that many SME owners intend to implement accounting by themselves or with an internal resource alone, giving up external support including help from consultants due to financial reasons. Though they might be able to afford help from these experts or external services as their scale grows, it is necessary to offer some support even for their self-sufficient efforts when the scale remains small. An effective option would be to develop and provide a guideline for keeping books and financial statements based on a given accounting standard to allow identification of what to do on what and how far by reading the guideline. Actually, responses from the subject countries for this research included: 'If only we have a comprehensive guideline...' The Philippines has already put the development/delivery of the easy-to-follow booklet on accounting for SMEs in place through the initiative of the government agency responsible for SME development. This would encourage the promotion of such a framework in other ASEAN countries.

The last option could be to develop a software accounting application that enables the utilisation of a simulated guideline feature using information and communication technology (ICT) and making it available for a reasonable cost for active use by SMEs. It would be ideal if the application creates books and financial statements for the user just by following a simple guiding wizard once installed in a PC. In Singapore, a respondent described a case where an application like this is also helping SMEs to work on accounting with relatively a small resource investment.

Thus, delivering relevant accounting information or applications may potentially wipe off the 'complicated and hard-to-understand' impression of accounting among SME owners, which will lead to the diligent use of accounting.

#### **4. Initiatives to be implemented by government bodies for execution of the Policy Options Proposal**

Government bodies will have to implement the following to execute the proposed

policy options 1 to 3:

(1) Collection of reality data in SME accounting

Our research is more or less working as the pioneering figure for data collection since some nations lack data such as how SMEs in particular are tackling or perceiving accounting. There were opinions recommending collecting as many data from a wide range as possible in the reality survey to allow productive discussions with institutes such as international organisations. It would work better if the surveys were pushed forward country by country, with dedicated focus on SME accounting for successful development and implementation of effective policies tailored to individual countries.

(2) Reflection of SME voices onto government policies

It would be ideal if opportunities are created to directly absorb thoughts, concerns and expectations on SMEs on accounting, on top of collection of reality data of SMEs. Voices heard from the subject countries for this research included 'No opportunities are available for SMEs to get heard on formulation of accounting rules including accounting standards' or, if available, 'The panel does not include a member who can represent SME claims'.

Since the growth of SMEs is indispensable to each ASEAN nation's national development, it is essential to get ready to proactively listen to SME voices on accounting as well.

(3) Propelling collaboration between government agencies and relevant organisations

Though different countries have different policies for SME accounting, it is highly necessary for multiple government bodies to work interactively. For example, interactive collaboration involving agencies responsible for SMEs or industry development, agencies (or organisations) controlling the accounting systems, internal revenue service agency as well as the ministry of education for the education of accounting personnel, will lead to effective policies implemented by the country.

Actually, during our research, some respondents pointed out that because of similar

education initiatives implemented by many different agencies, it is hard to see which agency is doing what on what. For example, policies that offer preferential loan interest rate based on diligent keeping of books and financial statements conforming to the accounting standard can be enabled by collaborating beyond agency borders.

## **5. Conclusion**

Our survey succeeded in qualitatively understanding, analysing, and summarising the accounting systems and status of compliance of SMEs mainly through desk research and field research on business operators, government agencies, and financial institutions in ASEAN countries.

We hope that this survey will offer an opportunity for the whole ASEAN region, governments of ASEAN countries, financial institutions, financial professionals, educational institutions, and business owners of SMEs in the ASEAN countries to collaborate with one another and deepen discussion. We further hope that the quality of management of SMEs and their access to finances will be improved.

- Ministry of Economy, Trade and Industry of Japan (2011), Field Survey of Japanese SMEs' accounting status. Available at: [http://www.chusho.meti.go.jp/zaimu/kaikei/2011/download/0823kaikei\\_enquete-1.pdf](http://www.chusho.meti.go.jp/zaimu/kaikei/2011/download/0823kaikei_enquete-1.pdf) (Japanese site only)
- Monileak, S. (2015), *Understanding the Accounting for Small- and Medium-Sized Enterprises in Cambodia*
- Pricewaterhouse Coopers (2001), *Transparency Project*
- Putranto, F. (2015), *Challenges of Accounting Standard for SMEs in Indonesia*
- Royal Government of Cambodia (2005), *Sub-committee on Small and Medium Enterprises, Small and Medium Enterprise Development Framework*
- Russell Bedford KTC (2015), *Vietnamese Accounting Standards (VAS)*. Available at: [http://russellbedford.vn/index.php?option=com\\_content&view=article&id=63:vietnamese-accounting-standards-qvasq&catid=8:accounting&Itemid=19](http://russellbedford.vn/index.php?option=com_content&view=article&id=63:vietnamese-accounting-standards-qvasq&catid=8:accounting&Itemid=19)
- Sakamoto, N. (2015), *Accounting for MSME in the Republic of the Philippines*. National Accounting Council of Cambodia (2006), MEF, *Article 2, Prakas No.431*,
- Small and Medium Enterprise Agency of Japan (2014), *65 Selected Cases of Companies Tackling the Standard for Small and Medium Enterprise*, March 2014. Available at: <http://www.chusho.meti.go.jp/pamflet/pamflet/2014/140304kaikei.pdf> (Japanese site only)
- Takeda, R. (2003), *SME Accounting, Analysis of the Small and Medium Enterprise Agency, Report of the Study Group on SME Accounting*, Chuo Keizai-sha
- Tao Jing (2014), *A study of small business accounting standards in China*, Doshisha Shogaku (The Doshisha Business Review) Available at: <http://ci.nii.ac.jp/naid/110009768138>
- The IFRS Foundation (2014), *Minutes of the 14th AEM-METI Economic and Industrial Cooperation Committee SME Working Group*
- Thomson Reuters (2014), *The AICPA's Financial Reporting Framework for Small- and Medium-Sized Entities - An Update*. Available at: <http://www.accountingweb.com/technology/accounting-software/survey-almost-half-of-cpas-know-about-aicpa-frf-for-smes>