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Factors Influencing the Adoption of International Financial Reporting Standards for Small and Medium Enterprises (IFRS for SMES): The Case of SMEs in Addis Ababa, Ethiopia

By  
Desta Amenu

Advisor  
Tekalign Nega (PhD)

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Addis Ababa, Ethiopia

**Addis Ababa University**  
**College of Business and Economics**  
**Department of Accounting and Finance**

**STATEMENT OF DECLARATION**

I, Desta Amenu, hereby declare that the thesis entitled Factors Affecting the Adoption of International Financial Reporting Standard by SMEs in Addis Ababa, Ethiopia is the outcome of my own effort and study and that all sources of materials used for the study have been properly acknowledged. This study has not been submitted for any degree in this University or other Universities.

Name: Desta Amenu

Advisor's Name: Tekalign Nega (PhD)

Signature: \_\_\_\_\_

**Addis Ababa University**

**College of Business and Economics**

**Department of Accounting and Finance**

**CERTIFICATION**

This is to certify that the thesis prepared by Desta Amenu, entitled: Factors Affecting the Adoption of International Financial Reporting Standard by SMEs in Addis Ababa; and submitted in partial fulfillment of the requirements for the degree of Master of Science in Accounting and Finance complies with the regulations of the University and meets the accepted standards concerning originality and quality.

Approved by:

External Examiner: \_\_\_\_\_ Signature \_\_\_\_\_ Date \_\_\_\_\_

Internal Examiner: \_\_\_\_\_ Signature \_\_\_\_\_ Date \_\_\_\_\_

Advisor:     Tekalegn Nega (PhD)

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# TABLE OF CONTENTS

ACKNOWLEDGEMENT .....	i
TABLE OF CONTENTS.....	ii
LIST OF TABLES.....	v
LIST OF ABBREVIATIONS .....	vi
ABSTRACT.....	vii
CHAPTER ONE.....	1
INTRODUCTION .....	1
1.1. Background of the study .....	1
1.2. Statement of the Problem.....	3
1.3. Research questions and hypothèses .....	4
1.3.1. Research questions.....	4
1.3.2. Research hypothesis.....	5
1.4. Objectives of the Study .....	8
1.4.1. General objective .....	8
1.4.2. Specific Objectives .....	8
1.5. Significance of the Study.....	9
1.6. Scope and Limitation of the Study.....	9
1.7. Organisation of the Study .....	10
CHAPTER TWO .....	11
RELATED LITERATURE REVIEW .....	11
2.1. Introduction.....	11
2.2. Theoretical Review .....	11
2.2.1. Institutional theory .....	11
2.2.2. Public interest theory .....	14
2.3. EMPIRICAL REVIEW .....	15
2.3.1. Relating to adoption of IFRS for SMEs.....	15
2.3.2. Relating to benefits of IFRS for SMEs adoption .....	15
2.3.3. Relating to factors affecting IFRS for SMEs adoption decision.....	16

2.4. International Financial Reporting Standards (IFRS) .....	22
2.5. International Financial Reporting Standard for Small and Medium Enterprises (IFRS for SMEs) .....	23
2.6. Small and medium-size Enterprises (SMEs) .....	23
2.7. Summary of literature and Research gap .....	26
2.8. Conceptual Framework .....	27
CHAPTER THREE .....	29
RESEARCH METHODOLOGY .....	29
3.1. Introduction .....	29
3.2. Research methods/approaches .....	29
3.3. Research design .....	30
3.4. Sources of research data collection .....	31
3.5. Research instruments .....	31
3.5.1. Semi-structured interview .....	31
3.5.2. Questionnaire Survey .....	31
3.6. Target population .....	32
3.7. Sample selection and size .....	32
3.8. Regression Analysis model of the study .....	33
3.9. Measurement of Variables .....	34
3.10. Data collection procedure .....	35
3.11. Reliability of Instrument .....	36
3.12. Construct Validity .....	36
3.13. Methods of Data Analysis .....	38
CHAPTER FOUR .....	39
DATA PRESENTATIONS, ANALYSIS AND DISCUSSIONS .....	39
4.1. Introduction .....	39
4.2. Data Presentation .....	39
4.2.1. Demographic features of respondents .....	39
4.2.2. Descriptive statistics on IFRS for SMES adoption level .....	40
4.2.3. Descriptive statistics to answer research questions .....	41
4.3. Results of logistic regression analysis to test research hypothesis .....	49

4.3.1. Diagnostic of Goodness-of-fit test .....	50
4.3.2. Diagnostic of Multicollinearity test .....	50
4.3.3. Result of main analysis of logistic regression.....	51
CHAPTER FIVE .....	55
SUMMARY OF MAJOR FINDINGS, CONCLUSION AND RECOMMENDATIONS .....	55
5.1. Introduction.....	55
5.2. Summary of Major Findings.....	55
5.3. Implication of the study .....	57
5.4. Conclusion .....	59
5.5. Recommendations.....	59
5.6. Recommendations for future research .....	60
REFERENCES .....	61
APPENDIX.....	ii

## LIST OF TABLES

Table 1 Definition of small and medium enterprises in Ethiopia.....	26
Table 2 Reliability Test (Cronbach's Alpha) .....	40
Table 3 Component matrix of Awareness of IFRS for SMEs .....	41
Table 4 Component matrix of education and training .....	41
Table 5 Component matrix of cost of conversion.....	41
Table 6 Component matrix of role and enforcement strategy of regulatory body.....	42
Table 7 Demographic features of respondents.....	43
Table 8 IFRS for SMES adoption level .....	45
Table 9 Descriptive statistics: To what extent company's awareness of IFRS for SMEs affects SMEs adoption decision in Ethiopia? .....	45
Table 10 Descriptive statistics: what impact or aid does education level and training have on IFRS for SMEs adoption decision?.....	47
Table 11 Descriptive statistics: To what extent that IFRS for SMEs conversion cost affects adoption decision by SMEs in Ethiopia?.....	49
Table 12 Descriptive statistics: What is the likelihood that role and enforcement strategy of regulatory body affects the IFRS for SMEs adoption decision? .....	51
Table 13 Descriptive statistics: What significant role does firm size play in the relationship between adoption decision and adoption challenge factors?.....	53
Table 14 Pearson correlation coefficient test.....	54
Table 15 Collinearity test Tolerance and Variance Inflation Factor (VIF) .....	55
Table 16 Logistic regression result of the model1 .....	55
Table 17 Logistic regression result of the model2.....	60

## **LIST OF ABBREVIATIONS**

AABE	Accounting and Auditing Board of Ethiopia
FASB	Financial Accounting Standards Board
GAAP	Generally Accepted Accounting Standards
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
IFRS for SMEs	International Financial Reporting Standard for Small and Medium Enterprises
SMEs	Small and Medium Enterprises

## ABSTRACT

*The International Accounting Standards Board (IASB), in its objectives, supposes that the beneficial effects from IFRS adoption include transparency, accounting quality and reduced cost of capital. In the year 2014, the Ethiopian government decided to adopt International Financial Reporting Standard for small and medium enterprises (IFRS for SMEs). This study examines factors that affect the adoption of International Financial Reporting Standard for Small and Medium Enterprises (IFRS for SMEs): The Case of SMEs in Addis Ababa, Ethiopia. The study employed explanatory survey design incorporating mixed research approach. The stratified random sampling technique across five sectors was used. To obtain answers to the research questions, questionnaires were distributed seeking the opinion of respondents. A total of 375 questionnaires were distributed. Out of which 232 was returned. The questionnaire data were analyzed using descriptive statistics and inferential statistics. Data from interviews were interpreted qualitatively. Quantitative data collected was analyzed with STATA Version 14.0 and logistic regression analysis was employed. The results of the study showed that most SMEs employees lacked awareness about IFRS for SMEs. The study results also revealed that size of a firm, lack of accounting education and inefficient practical training are among the factors that influences the adoption of IFRS for SMEs. Little or no effort is being made by regulatory body to monitor, review and enforce SMEs to adopt the standard in the SMEs sector. Overall, the findings of the study showed that the majority of SMEs in Addis Ababa are not ready to adopt this standard yet. The study recommends SMEs to do their best in developing awareness of their employees towards the standard through organizing the necessary training, accessing materials from internet and made available them in the working environment and also AABE should do enforcement activities through onsite inspection and other mechanisms such as collaborating with banks and Ethiopian Ministry of Revenue to ensure successful adoption of the standard.*

**Keywords:** Financial Reporting, the Standard, IFRS for SMEs, SMEs, AABE.

# CHAPTER ONE

## INTRODUCTION

### 1.1. Background of the study

Today developing and emerging markets and economies are the targets of the world's leading industries. Since these foreign investors may demand comprehensive financial information and foreign investments greatly contribute to the development of economy of a country, developing countries should adopt international accounting standard (Zeghal & Mehdhbi, 2006).

Ethiopia is one of the sub-Saharan African developing countries with world's fastest growing economy (IMF, 2019), has been looking for World Trade Organization (WTO) membership since 2003. Currently, the government has made WTO membership and the African Continental Free Trade Area (ACFTA) a priority in its Homegrown Economic Reform Plan and aims to accelerate the WTO accession process for conclusion by end of 2021. Hence, the country needs quality financial information to benefit from the international markets and to access international financing sources by adopting and implementing international accounting standards such as International Financial Reporting Standards (full IFRS), International Financial Reporting Standards for Small and Medium Enterprises (IFRS for SMEs) and International Public Sector Accounting Standard (IPSAS). This study concerned with examining the factors that affects adoption of IFRS for SMEs by small and medium enterprises (SMEs) in Addis Ababa, Ethiopia, a standard issued by International Accounting Standards Board (IASB) for Small and medium enterprises (SMEs).

SMEs play important role in the economic development of every country throughout the world. In Ethiopia, the collective contribution of SMEs sector is evaluated by its potential of creating employment opportunities for skilled and unskilled human power. In this study the size of SMEs was determined by total annual turnover/sales, total assets, total liability and number of employees (AABE, 2017).

To enable SMEs to have international look, International Accounting Standard Board (IASB) issued IFRS for SMEs for small and medium enterprises on July 9, 2009. This standard provides

an alternative framework that can be applied by eligible entities in place of fullest of IFRS for SMEs in issue (Deloitte, 2009).

Previous studies on the adoption of IFRS for SMEs in different countries conducted by Albu (2013), Quagli & Paoloni (2012), Hussain, F., Chand, P., & Rani, P. (2012), Eierle & Haller (2009), Masca (2012) showed that the adoption of IFRS for SMEs in Europe is influenced by accounting culture of the geographical area in which they operate, the implementation of IFRS for SMEs poses a challenge for practitioners such as meeting the standard, training requirements, and size influenced the suitability of IFRS for SMEs (UNCTAD, 2016).

Studies conducted by other researchers like Alp & Ustundag (2009), Irvine & Lukas (2006) and the United Nations Conference on Trade and Development UNCTAD (2007a), noted that capacity related issues, lack of accounting education and training are some of the challenges resulting from adoption of IFRS for SMEs.

Despite the fact that a number of researchers investigated the adoption and implementation challenges of IFRS for SMEs, most of them were conducted in Europe. However, as far as the knowledge of the researcher is concerned, very few research has been conducted in developing countries particularly in Africa like Rudzani & Charles (2016), Arhin, Perprem & Hulede (2017), Ezeagba (2017), Keneth & Grazyina (2013), Chege & Muturi (2016) and no research in Ethiopia related to the topic under consideration. Moreover, there is a perception that SMEs, especially in developing countries may not have sufficient knowledge, skills and resources to adopt and implement IFRS for SMEs and benefit from the use of the standard. As per the knowledge of the researcher, there are no previous studies conducted by collecting data from SMEs in Ethiopia, particularly SMEs in Addis Ababa regarding factors affecting the adoption of IFRS for SMEs by SMEs in Addis Ababa, based on education level and training, awareness level, enforcement strategies, cost of conversion and size as a mediation factor between adoption decision and adoption influencing factors.

The aim of this study, therefore, is to bridge this gap and tries to analyze the challenges that SMEs in Ethiopia faces and identify main factors that affect the adoption of IFRS for SMEs, particularly SMEs in Addis Ababa.

## **1.2. Statement of the Problem**

According to IASB (2009a), IASB believes that adopting IFRS for SMEs helps SMEs access to global finance through harmonized and high quality financial information. In order to produce high quality financial information, ISAB published in July 2009 self-contained and comprehensive accounting standards for SMEs, the IFRS for SMEs regulations. IFRS for SMEs are simplified version of full IFRS which is primarily based on fundamental principles of full IFRS (ISAB, 2009 b).

Several developed and developing countries have actually adopted IFRS for SMEs and others have plans to adopt the standard. The issue of benefits and challenges of adopting IFRS for SMEs in developed countries have already been studied, but very few studies have been conducted in developing countries in Africa, particularly in Ethiopia. Prior researches in Ethiopia have focused on the challenges or factors affecting the adoption of full IFRS (Arefainie, 2018; Hache, 2019; Alemgena, 2016; Fikru, 2012; Melese, 2016; Firdawek, 2017).

With regard to the adoption of the standard, some studies focused on the analysis of the benefits of adopting IFRS for SMEs such as improved financial reporting, comparability of financial information of SMEs, easy access to finance, investor confidence, proper compliance with tax regulations (Rudzani et al., 2016; Ezeagba, 2017; Panagiotidou, 2015; Mazhindu et al., 2013; Chege et al., 2016).

Despite the benefits it has, there are factors that affect IFRS for SMEs adoption decision. Out of the previous studies, most of them examined the challenges or factors affecting adoption of IFRS for SMEs as lack of awareness, lack of technical skills, high cost of implementation, education level, but few have tried to examine firm size (Panagiotidou, 2015; Chege et al., 2016; Mazhindu et al., 2013; Kuqi & Jonuzi, 2011). Kuqi & Jonuzi (2011) also provided a recommendation on further study if the size of the enterprise would be an advantage or disadvantage in using IFRS for SMEs. To the researcher knowledge, a report by Mukokoma & Tushabomwe-Kazooba (2019) is the only study prepared as a report that examined the firm size as mediation influence on the relationship between adoption decision and enablers and inhibitors. Moreover, there is no empirical research focusing on the effect of regulatory body enforcement strategy on SMEs decision to adopt IFRES for SMEs. Unlike previous studies, this study include factors such as

enforcement strategy of regulatory body and the mediation influence of firm size between adoption influencing factors and SMEs adoption decision, to better examine them in the context of Ethiopian economy.

The Various challenges reported by previous studies on the adoption of IFRS for SMEs vary by countries, so that cannot be generalized and generalizing of these challenges may not bring possible solution to specific country like Ethiopia. As far as the knowledge of the researcher is concerned, in the case of Ethiopia, the major factors of adopting IFRS across SMEs have not been clearly identified. However, a study conducted by Tseganesh (2019) on implementation progress of IFRS for SMEs in Woliata Sodo Town (from owner-managers' perspective) discusses challenges of adopting IFRS for SMEs in terms of lack of awareness on financial accounting standard, lack of information on IFRS.

This study, therefore, aims to examine factors affecting the adoption of IFRS for SMEs by SMEs in Addis Ababa, Ethiopia. Specifically, the study examines how lack of awareness, education level and training, cost of adoption, and role and enforcement strategy of regulatory body affects the IFRS for SMEs adoption decision. The study also examines how firm size is considered as a mediation influence factor between SMEs adoption decision and major factors affecting adoption of IFRS for SMEs.

### **1.3. Research questions and hypotheses**

#### **1.3.1. Research questions**

The aim of this research was to analyze how lack of awareness, education level and training, cost of adoption, and role and enforcement strategy of regulatory body and firm size as mediation factor affects the adoption of IFRS for SMEs by SMEs in Addis Ababa, Ethiopia. Therefore, the general question of this research is what are the factors that affect the adoption of IFRS for SMEs? Based on this general question, the following specific questions were examined:

- Q1. To what extent does awareness of IFRS for SMEs affects SMEs adoption decision in Ethiopia?
- Q2. What impact do educational qualification level and training have on IFRS for SMEs adoption decision?

Q3. To what extent does cost of conversion affects IFRS for SMES adoption decision in Ethiopia?

Q4. What is the likelihood that role and enforcement strategy of regulatory body affect the IFRS for SMEs adoption decision?

Q5. What significant role does firm size play as a mediation influence in the relationship between adoption decision and adoption challenge factors?

### **1.3.2. Research hypothesis**

A hypothesis is a tentative statement of fact that is yet to be verified by the researcher Frank, 1979 (as cited in Mazhindu et al., 2013). In this study, in order to address the various research questions that could explain the adoption and implementation of IFRS for SMEs four independent variables and one mediating variable against one dependent variable was developed and analyzed. The independent variables are awareness of IFRS for SMEs education qualification level and training, cost of conversion, role and enforcement strategies of regulatory body, and size of SMEs mediating variable, while the dependent variable is adoption IFRS for SMEs.

Considering the impact of independent variable on the dependent variable, the following research hypotheses were developed and analyzed.

#### **1. Awareness of IFRS for SMEs (H1)**

The result of the survey by Deloitte (2009) revealed that 43% of SMEs respondents were not aware of the IASB's standard IFRS for SMEs. Most businesses still do not understand what options are available and how IFRS for SMEs interplay to their benefits (Fortuin, 2011). This is an indication of lack of awareness of the benefits accrued through the use of IFRS for SMEs which may intern inhibits SMEs from adopting them. Therefore, the following relationship is hypothesized.

H1: Awareness of IFRS for SMEs has significant effect on the decision to adopt IFRS for SMEs

## 2. Education level and training (Normative Isomorphism theory) (H2)

Within institutional theory, education and training quality are normative pressures that explain the emergence and development of many practices such as accounting one (DiMaggio & Powell, 1983; Meyer & Rowan, 1977 cited in Sellami and Gafsi 2018).

According to Chand & White (2015) (cited in Sellami and Gafsi, 2018), several developing countries still face challenges in implementing IFRS for SMEs due to lack of adequate accounting training, limited professional capacities and high training costs that are major factor hindering the adoption and implementation of IFRS for SMEs. On the other hand, accountants and practioner in Big 4 firms have played a supporting role in properly implementing IFRS for SMEs in many past developers like Fiji because they have high quality training and sufficient expertise (Hussain et al., 2012). However, a study conducted by Kaya & Koch (2015) showed that there is no relationship between education level and the decision of adopting IFRS for SMEs. This shows that there is inconsistency of research results. Therefore, the following relationship is hypothesized:

H2: Education level and training has significant effect on the decision to adopt IFRS for SMEs

## 3. Cost of conversion (H3)

It is not an easy task for SMEs to adopt IFRS for SMEs since they cannot do it by themselves. They are required to hire the services of expertise, which cost the SMEs a lot. A number of studies conducted in different countries witnessed this. IFRS for SMEs too costly to apply and SMEs reporting entities are more concerned about the costs associated with conversion rather than the benefits obtained from using the standard (Hussain et al., 2012; Litjens, S., & Vergoossen, 2012). However, a study conducted by Albu et al. (2013) stated that stakeholders do not recognize the implementation of IFRS for SMEs as a cost burden rather considered it as an opportunity to make better the business environment by training accountants and disclosing a quality accounting information. This implies that the impact of conversion cost and IFRS for SMES adoption decisions are not consistent across different studies.

Investigation of the association between IFRS for SMEs adoption and conversion cost is proposed to contribute to an understanding of the factors that impact or aid the successful adoption of IFRS for SMEs. Therefore, the following relationship is hypothesized.

H3: Cost of conversion has significant effect on the decision to adopt IFRS for SMEs

#### 4. Role and enforcement strategy of regulatory body (Coercive Isomorphism theory) (H4)

According to DiMaggio and Powell (1983), coercive isomorphism involves a regulation that forces organizations to adopt a particular practice. Under institutional theory, coercive isomorphism results from external pressure and certain practices that are adopted as a result of governments', capital markets' pressures or the expectations of the larger society. Coercive isomorphism takes the shape of a formal or an informal pressure exerted on an organization by other superior organizations upon which they depend as well as the cultural environment within which an organization operates. In most instances, such pressures might be perceived by the organizations as force, persuasion or an invitation to adopt a particular policy (Rodrigues & Craig, 2007).

The main institution that might have internally influenced the adoption of International Financial Reporting Standards in Ethiopia is AABE. This institution influences the choice of reporting standards that are used in Ethiopia as a member of International Federation of Accountants (IFAC). According to AABE, there are three phase roadmaps for mandatory adoption of IFRS. The roadmap enforces enterprises to adopt and implement IFRS as early as possible.

Moreover, Mazhindu et al. (2013) and Albu et al. (2010) noted that in Africa, the incapacity to enforce by the regulatory body is the major factor that hinders the adoption and implementation of IFRS for SMEs as compared to the lack of ability to adopt the standard. Following this logic, we expect that a decision by SMEs not to adopt IFRS for SMEs may be significant for country with poor enforcement strategy. Therefore, the following relationship is hypothesized:

H4: Role and enforcement strategy of regulatory body has significant effect on the decision to adopt IFRS for SMEs

## 5. Size of firm (H5)

Size is usually measured by the number of employees, capital, annual sales and total assets. The use of quantified criteria like these ones in deciding the scope of standards creates clarity for all stakeholders (Jarvis & Collis, IFRS and Differential Reporting., 2003). Quantitative criteria for differential reporting are already used in various countries (Jarvis et al., 2003) and seem to be the preferred approach for deciding the scope of a possible implementation of the IFRS for SMEs (Bunea& M., Quagli et al., 2012). However, a study conducted by Eierle& Haller (2009) noted that there is no significant relationship between size and assessment of accounting methods. On the other hand, according to IASC Foundation (2009b: BC63) size is not necessarily associated with accountability. Therefore, the following relationship is hypothesized:

H5: Size of SMEs has mediation influence on the relationship between adoption decision and adoption challenge factors

### **1.4. Objectives of the Study**

#### **1.4.1. General objective**

The general objective of the research was to analyze factors that affect adoption of IFRS for SMEs by SMEs in Addis Ababa, Ethiopia.

#### **1.4.2. Specific Objectives**

The specific objectives of the research are:

1. To analyze how awareness affects the adoption of IFRS for SMES by SMEs in Ethiopia
2. To determine how education level and training affects the adoption of IFRS for SMEs by SMEs in Ethiopia.
3. To determine the effect of cost of conversion on the decision to adopt IFRS for SMES by SMEs in Ethiopia.
4. To assess how regulatory body enforcement strategy influence IFRS for SMEs adoption decision by SMEs in Ethiopia
5. To assess the mediation influence of firm size between adoption challenge factors and SMEs adoption decision

## **1.5. Significance of the Study**

The findings of the study will provide useful and timely information to the regulatory body in its oversight activities with regard to the enforcement strategy of the adoption and implementation of IFRS for SMEs by SMEs.

The result of this research will also assist domestic and international standard setting agencies, and the accounting profession, to understand the firm characteristics and environmental factors influencing the successful adoption of IFRS for SMEs in developing countries, especially in Ethiopia.

The findings of the study might also provide practitioners and researchers an understanding of the adoption of IFRS for SMEs situation in developing countries particularly in Ethiopian context.

## **1.6. Scope and Limitation of the Study**

According to Accounting and Auditing Board of Ethiopia (AABE), under phase III category of the roadmap, Small and Medium-Sized Entities (SMEs) are required to follow IFRS for SMEs, a simplified self-contained standard, by the end of 2018. If at least two of the following requirements are fulfilled the firm falls into phase III category: Between 1 million - 50 million annual turnover/sales or Between 10 - 100 employees or Between 2 million -100 million Total Asset or Between 2 million -100 million Total Liability. Thus, this research study only focused on small and medium enterprises in Addis Ababa that fulfill the above requirements due to time and financial constraints and the sample of SMEs was drawn from this target group of entities. The study focused on the adoption of IFRS for SMEs which is one version of the IFRS, but full IFRS and IPSAS are out of the scope of this study. The study has two limitations. First, because of lack of cooperation and commitment among respondents and COVID-19 outbreak, not all questionnaires were collected. Second, there was lack of empirical studies on factors affecting adoption of IFRS for SMEs by SMEs in Ethiopia during the study.

## **1.7. Organisation of the Study**

This paper is organized into five chapters. The first chapter presents introduction, which consists of background, statement of the problem, objective of the study, research hypothesis, scope of the study, significance of the study, and organization of the paper. The second chapter deals with the literature review which consists of review of theories, empirical literature review and conceptual framework of the study. The third chapter deals with research methodology. The fourth chapter deals with analysis and discussion of data collected. The fifth chapter deals with summary of major findings, conclusion and recommendations.

## **CHAPTER TWO**

### **RELATED LITERATURE REVIEW**

#### **2.1. Introduction**

This chapter of the literature review is based on the study and review of existing and previous theories related to the research area selected for the study. The remainder of the chapter is divided into four sections. The first section consists of the relevant theories of accounting practice and international accounting standards' adoption that form the study, the second section is regarding reviews of the related previous literatures on IFRS for SMEs adoption challenge factors and the last section is conceptual framework of the study.

#### **2.2. Theoretical Review**

This section attempts to review literatures which consider theories explaining need for accounting standards in SMEs situation. For this study, the two theories that are most relevant to adoption of IFRS for SMEs are public interest and positive accounting.

##### **2.2.1. Institutional theory**

According to Guerreiro (2012), the institutional theory explains why organizations adopt certain accounting standards to bring about legitimacy to the organization or to respond to institutional pressure. The institutional framework explains the mechanisms through which organizations seek to align perception of their practices and characteristics with the social environment, and how such practices become institutionalized in a particular organization (Deegan & Uneman, 2006). A development of the institutional theory was envisaged in order to facilitate the understanding of change. DiMaggio and Powell (1983) identify three mechanisms through which institutional change occurs: coercive, mimetic and normative.

Rodriguez et al., (2007) also develop a framework to study accounting harmonization integrating the three forms of isomorphism (coercive, normative and mimetic). Potter (2005) builds on Miller (1994) a framework to study accounting as a social and institutional practice.

The theory of isomorphism defines the “constraining process that forces one unit in a population to resemble other units that face the same set of environmental conditions” (Hawley (1968) cited in DiMaggio & Powell 1983).

DiMaggio and Powell (1983) assert that “organizational characteristics are modified in the direction of increasing compatibility with environmental characteristics; the number of organizations in a population is a function of environmental carrying capacity; and the diversity of organizational forms is isomorphic to the environment diversity.” This theory in practice implies that, the features of an organization, for example SMEs in Ethiopia, can be adjusted to some extent for the sake of compatibility and uniformity to suit the surrounding environment of the organization which is the global world.

#### **2.2.1.1. Coercive isomorphism**

According to DiMaggio and Powel (1983) a regulation that forces organizations to adopt a particular practice is features of coercive isomorphism.

Coercive isomorphism results from external pressure and certain practices that are adopted as a result of governments’, capital markets’ pressures or the expectations of the larger society. This form of isomorphism stems from political influence and the problem of legitimacy. Coercive isomorphism takes the shape of a formal or an informal pressure exerted on an organization by other superior organizations upon which they depend as well as the cultural environment within which an organization operates. In most instances, such pressures might be perceived by the organizations as force, persuasion or an invitation to adopt a particular policy (Gasi, 2010). The main institution that might have internally influenced the adoption of International Financial Reporting Standards in Ethiopia is AABEE. This institution influences the choice of reporting standards that are used in Ethiopia as a member of International Federation of Accountants (IFAC).

#### **2.2.1.2. Mimetic isomorphism**

According to DiMaggio & Powell (1983), Mimetic isomorphism is seen as adopting best practices in order to be more legitimate or successful. Mimetic isomorphism exists when organization copy the activities of other organization during uncertainty. The degree of uncertainty of an existing practice is a powerful force that encourages imitation. Therefore, one

can be argued that SMEs in developing countries would mimic or copy the activities, standards, and principles of successful developed countries when they are uncertain about the effects that their current principles might have on their organization in the future (DiMaggio & Powell, 1983).

Previous studies Vivian & Ehsan, (2001) and Khadaroo (2005) found out an evidence of mimetic change in examining the adoption of new practices of organizations.

The IASB gives two optional approaches to implement IFRS by a particular jurisdiction: totaling and customizing approaches. The first approach is known as adoption or “big bang” approach while the latter is called a convergence approach. “Big bang” approach is a strategic decision to adopt IFRS on a single date or, perhaps, a series of dates applied to firms of different sizes. While in convergence approach, gradual movement is made towards IFRS through customizing with the existing accounting standards and IFRS are applied gradually (IFRS Foundation Guide, 2013).

Ethiopia changes its accounting system previously guided by no local standard to IFRS. In the year 2014, the government of Ethiopia officially announced the adoption of IFRS (full IFRS, IFRS for SMEs and IPSAS) for the financial accounting and reporting practice in the country (Proclamation No. 847/2014). The Accounting and Auditing Board of Ethiopia (AABE) was established in the year 2014 by the Council of Ministers as autonomous legal body to oversight the accounting and auditing professions and financial reporting practice in Ethiopia (Ethiopian Government 2014). Before the establishment of AABE, there had been no single organized body responsible for regulating the accounting and auditing professions and financial reporting practices in Ethiopia (Alemi and Pasrisha 2016).

The above-mentioned problems together with others of vital importance to the economy of Ethiopia created uncertainty in the accounting profession. To remedy this situation, a solution in the form of adopting the International Financial Reporting Standards (IFRS or IFRS for SMEs) became necessary.

### **2.2.1.3. Normative isomorphism**

Normative isomorphism was the last application of isomorphism within institutional theory and derived primarily from process of professionalization. DiMaggio and Powell (1991) argue that, organizations adopt what they believe are best practices as certified by professional body to become more successful. The degree of professional technical knowledge of a nation has a positive relationship with its ability to adapt to standards that are of good quality and internationally recognized which were facilitated by professional standards. Therefore, a Nation's attainment of education may spark normative pressures birthed by professionalism (Guler, Guillen, & Macpherson, 2002).

Institutional theory has been extensively used in analyzing IFRSs implementation and/or accounting change because it emphasizes the importance of institutions, beliefs, rules, routines, and culture (Dillard, Rigsby, & Goodman, 2004). Normative isomorphism is attributable to professionalization. Professionalization is defined to be the collective struggle of members and an occupation to define the conditions and methods of their work, to control the "production of producers" and to establish a cognitive base and legitimization for their occupational autonomy (Larson 1977 cited in DiMaggio and Powell 1983). This emphasizes that professional bodies are a group of individuals with common interest and aspirations. They therefore strive together to circulate these common objectives they possess, design criteria for application of membership, and set limits as to the quantity of members at each point in time.

### **2.2.2. Public interest theory**

According to Kumekewa (2017) public interest theory has no clear origin but can be traced to the works of Pigou in 1902 who related his works to externalities and welfare economics. According to the theory, regulation is assumed to benefit stakeholders by balancing regulatory costs and benefits. Under the public interest theory, regulation is a socially efficient response to market failures such as natural monopoly, externalities, information asymmetries, and excess competition. Kothari, Ramanna, & Skinner (2010) argue that information asymmetries are particularly relevant to justify financial disclosure regulation, but less compelling in justifying regulation of GAAP. The authors emphasize that accounting information has the feature of a public good.

In order to meet the informational demands of different parties, the government –regulated supply of accounting information has been necessary. Since Ethiopia does not have national accounting standards previously, internationally acceptable accounting standards can serve the public interest by enhancing the quality and credibility of accounting information to external parties and also internally to firms’ managers.

## **2.3. EMPIRICAL REVIEW**

### **2.3.1. Relating to adoption of IFRS for SMEs**

According to the United Nations (2008) the concept of applying global reporting standards to SMEs in developing countries is believed to be more difficult than elsewhere. While the adoption of IFRS for SMEs seems reasonable for developed countries, developing countries might not be able to exercise the same expected economic benefits enjoyed by developed economies due to certain distinctiveness of their accounting and business infrastructure. For instance, lack of skills and knowledge of their accounting professions; smaller and less developed capital markets; lower level of governance; and limited numbers of international business participants.

### **2.3.2. Relating to benefits of IFRS for SMEs adoption**

According to studies a number of benefits encourage SMEs to adopt IFRS for SMEs. Frinewater house coopers (2006) and IASB (2009) noted that the benefits of the IFRS for SMEs are as follows; Adoption of IFRS for SMEs will improve the comparability of financial information of SMEs to either national or international level, Building the confidence of suppliers on the quality of information reported, Adoption of IFRS for SMEs will make easier to implement planned cross-border acquisitions and to initiate proposed partnership with foreign entities, Adoption of IFRS for SMEs will have a positive effect on the credit rating scores of enterprises, this will strength SMEs relationship with credit institutions, Adoption of IFRS for SMES will attract ventures capital investors in SMEs from other countries, The adoption of IFRS will enhance the financial health of the SMEs, For SMEs where ownership and management are separate, adoption of the standards would give owners confidence in the reported financial figures.

Adoption of IFRS for SMES benefits users and prepares in a number of ways such as, increased level of transparency, increased comparability of financial statements information, better access to the global capital market (Iyoha & Fboyede, 2011; Apostolos, Despina & Christos, 2010; Jermakowicz & Gornik-Tomaszewki, 2007).

According to Bohusova (2011), studies made in less developed countries such as Kenya, South Africa, Turkey and Ghana indicated that the adoption of IFRS for SMES would improve their access to financial funds, would help them to enter international markets and their financial performance would be improved. Therefore, adoption of IFRS for SMEs in Ethiopia would not be exceptional to this. Currently, Ethiopia is on the way to be a member of World Trade Organization (WTO) so that adoption of IFRS for SMEs will facilitate this issue. Because of their size and lack of availability of in-house business skill, SMEs tend to operate locally and are not interested in international business (Lungu et al., 2007). Thus, it is claimed that there is no benefit for entities that operate locally to follow IFRS for SMEs (Jeman & Iyankovic, 2011).

### **2.3.3. Relating to factors affecting IFRS for SMEs adoption decision**

#### **2.3.3.1. Awareness of IFRS for SMEs**

Another factor affecting adoption of IFRS for SMEs is limited awareness of IFRS for SMEs. Most businesses still do not understand what options are available and how IFRS for SMEs inter play to their benefits (Fortuin, 2011). This is an indication of lack of awareness of the benefits accrued through the use of IFRS for SMEs which may intern inhibits SMEs from adopting them (Fortuin, 2011).

A study by Clementina, Egwi & Isu (2014) examined adoption challenges of limited awareness of IFRS for SMEs in Nigeria. The awareness challenges were related to failure by SMEs to get information about the standards. Additionally, the result of the survey by Deloitte in 2009 revealed that 43% of SMEs respondents were not aware of the IASB's standard IFRS for SMEs.

Wong (2004) argued that National professional accountancy bodies are required to create awareness and expand the knowledge of professional accountants and others on IFRS. According to Bhattacharjee & Hossain (2010) a number of reasons were provided for the low level of adoption of IFRS for SMEs. In this regard, a number of explanations were brought forth which

include unwillingness to work and accept a more principles-based set of accounting standards compared to the more rules-based IFRS (Adekoya, 2011).

### **2.3.3.2. Education level and training**

The typical owner or managers of small businesses develop their own approach to management, through the process of trial and error (Anderson, 1993). As a result, their management style is likely to be more intuitive than analytical, more concerned with day-to-day operations than long term issues, and more opportunistic than strategic in its concept. A consequence of poor managerial ability is that SMEs owners-managers are ill prepared to face changes to the business environment and to plan appropriate changes in technology and standards. Majority of those who run SMEs are ordinary lot whose educational background is lacking. Hence, they may not well equip to carry out managerial routines for their enterprises (King and McGrath, 2002).

Under institutional theory, education and training quality are normative pressures that explain emergence and development of many practices such as accounting ones (Meyer & Rowan, 1977; DiMaggio & Powell, 1983). Based on IFRS principles, IFRS for SMEs is a high quality standard that requires a high level of knowledge and deep accounting skills.

IASB (2004) noted that the biggest challenge that exists in implementing IFRS for SMEs is providing adequate training to equip practioners with the necessary skills before the first set of financials are prepared. The IASB board commented that accountants would need adequate training to understand the implications of using IFRS for SMEs in preparing financial statements IASB (2004).

According to various researches, accountants and their professional capacity play a crucial role, in which their assessment and professional judgment are the key factors (Bunea, 2006; Albu, 2010). As the direct producers of information, the professional competence and responsibility of the accounting department is positively correlated with the quality of information they provide. In the advent of inadequate professional capability, the deficient cognition of accountants can result in misinterpretation and incomplete utilization of the legal regulations; as a consequence, the implementation of these legal documents is inefficient. Considering such important role, accountants' skills in most enterprises are yet limited (Joshi & Ramadhan, 2002; Martin, 2005). Also in agreement with this viewpoint, the research result of Albu et al. (2010) in Romania

specified that accountants' capacity has a critical influence on the application of accounting standards into practice.

Dang-Duc (2011) also carried out a research to investigate the application of accounting standards in SMEs in Vietnam. The research findings revealed five major factors affecting this application, among which the mandatory compliance and external pressure on improved information are two key factors. Additionally, the deficiency in managing and accounting skills, lack of infrastructure, cost and benefit relationship and pressure on information are other factors that count. On the other hand, the major drawback of this research is its narrow sample and its primary concentration on accountants which are responsible for the incomplete generalization of this research.

Financial accounting standards are less developed when accountants have little experience and knowledge of complex accounting issues, and if the professional body is developed and strong, it is more likely to develop a sophisticated set of financial accounting standards (Ding, Hope, & Stolowy, 2007). Preparers of European countries say that IFRS for SMEs is not suitable in European context because of the difficulty in applying the standard, since it is too similar to Full IFRS despite efforts to simplify it (Quagli & Paoloni, 2012).

Since they have high quality training and sufficient expertise, accountants and practitioners in Big 4 firms have played a supporting role in properly adopting and implementing IFRS for SMEs in many past adopters like Fiji (Hussain et al., 2012). However, a study conducted by Kaya & Koch (2015) stated that there is no relationship between education level and the likelihood of adopting IFRS for SMEs. This shows that there is inconsistency of research results.

#### **2.3.3.3. Effect of cost of conversion on IFRS for SMEs implementation decision**

It is not an easy task for SMEs to adopt IFRS for SMEs since they cannot do it by themselves. They are required to hire the services of expertise, which cost the SMEs a lot. A number of studies conducted in different countries witnessed this. IFRS for SMEs too costly to apply and SMEs reporting entities are more concerned about the costs associated with conversion rather than the benefits obtained from using the standard (Hussain et al., 2012; Litjens et al., 2012). However, a study conducted by Albu (2013) stated that stakeholders do not recognize the implementation of IFRS for SMEs as a cost burden rather considered it as an opportunity to

make better the business environment by training accountants and disclosing a quality accounting information. This implies that the impact of conversion cost and IFRS for SMES adoption decisions are not consistent across different studies.

#### **2.3.3.4. Role and enforcement strategy of Regulatory body on SMEs adoption decision**

Within institutional theory, coercive isomorphism results from external pressures and certain practices that are adopted as a result of governments or capital market pressures (Rodrigues et al., 2007). Coercive isomorphism takes the shape of a formal or an informal pressure exerted on an organization by other superior organizations operates. In most instances, such pressures might be perceived by the organization as force, persuasion or an invitation to adopt a particular policy (Rodrigues et al., 2007).

Adoption and implementation of IFRS can be influenced by the enforcement mechanisms as well as corrective procedures that a responsible body will implement on non- conformity (Mir & Rahaman, 2005).

According to UNCTAD (2007), one of the critical elements in the adoption and implementation of IFRS is the rigorous enforcement of standards. The responsibility of enforcing IFRS rests with a number of parties. Institution such as securities exchange commission, banking and insurance supervisory authorities, stock exchange and capital market authorities play important roles in enforcing financial reporting requirements such as IFRS.

In South Africa, the Generally Accepted Accounting Principles (GAAP) Monitoring Panel, which was created by the South African Institute of Chartered Accountants and the Johannesburg Stock Exchange in 2002, is responsible for ensuring compliance with financial reporting standards. Prior to the creation of the panel, there was no regulatory enforcement of financial reporting standards. In Turkey, the Capital Markets Board is responsible for monitoring and enforcing listed firms' compliance with financial reporting standards (UNCTAD, 2006).

The main institution that might have internally influenced the adoption of IFRS in Ethiopia is Accounting and Auditing Board of Ethiopia (AABE). This institution influences the choice of reporting standards that are used in Ethiopia as a member of IFAC. Accounting and Auditing

Board of Ethiopia (AABE) was established under Regulation No. 332/2014 and it has issued the following IFRS implementation road map:

*Phase 1:* Significant Public Interest Entities (PIEs) - primarily financial institutions and federal public enterprises- are required to adopt IFRS standards from calendar year 2017, with reporting under IFRS starting in 2017.

*Phase 2:* Other PIEs-including ECX members- and private firms that meet the PIE thresholds criteria and IPSAS for Charities and Societies are required to report under IFRS by the end of 2018.If at least two of the following requirement is fulfilled the firm satisfied PIE qualitative thresholds and it falls into phase II category: greater than 50 million annual turnovers/sales or greater than 100 employees or greater than 100 million total assets or greater than 100 million total liabilities

*Phase 3:* Small and Medium-Sized Entities (SMEs) are required to adopt from July 8, 2018 and follow IFRS for SMEs, a simplified self-contained standard; by the end of 2019.If at least two of the following requirement is fulfilled the firm falls into phase III category:1) between 1 million &50 million annual turnover/sales 2) between 10 &100 employees 3) between 2 million & 100 million Total Assets 4) between 2 million & 100 million Total Liabilities.

Therefore, the role and enforcement capacity of AABE in collaboration with other institutions like Ethiopian Revenue Authority and banks on the effective adoption and implementation of IFRS for SMEs needs to be examined.

#### **2.3.3.5. The impact of size factor in the relationship between adoption challenge factors and SMEs adoption decision**

The scope of the IFRS for SMEs as issued by the IASB is defined to be entities that “do not have public accountability and publish general purpose financial statements for external users” (IASB Foundation, 2009a: par. 1.2.). In IASB’s view “size is not a barrier. Any firm of any size is eligible to use the IFRS for SMEs, provided it does not have public accountability” (IFRS Foundation, 2010). However, “in deciding which entities should be required or permitted to use

the IFRS for SMEs, jurisdictions may choose to prescribe quantified size criteria” (IASC Foundation, 2009b: BC70).

Size is usually measured by the number of employees, sales and total assets. The use of quantified criteria like these ones in deciding the scope of standards creates clarity for all stakeholders (Jarvis and Collis, 2003). Quantitative criteria for differential reporting are already used in various jurisdictions (Jarvis and Collis, 2003) and seem to be the preferred approach for deciding the scope of a possible implementation of the IFRS for SMEs (Bunea et al., 2012; Quagli et al., 2012). On the other hand, size is not necessarily associated with accountability (IASC Foundation, 2009b: BC63), and the quantitative approach, even if it seems objective, may be distorted (Bunea et al., 2012).

Albu (2013) investigated whether firm size is relevant in determining the scope of the IFRS for SMEs in Romania. The result showed that using only size as a criterion for setting the scope of the IFRS for SMEs may cause the exemption of a significant number of firms and therefore, may lead to compliance issues. Research conducted in Germany by Brigitte & Haller (2009) showed that size is only significant if the organization has cross border business transactions.

Aljifri and Khasharmeh (2006) cited in Litjenset al. (2012) found out that the level of international standards’ adoption is positively correlated with size, whereas, Dang (2011) concluded that the association between the size of business and compliance with accounting standards is not significant. Additionally, little research exists on how size affects the cost-benefit ratio in differential reporting (Jarvis & Collis, 2003).

Other authors Eierle et al. (2009) analyze through an empirical study conducted in Germany, the extent to which size is representative for the relevance of some accounting issues such as international exposure, the perception of preparers on the associated costs and benefits, but the results are ambiguous and the authors call for future studies. Because the previous results are limited or contrasting, there is an important call for more empirical studies in this domain. Furthermore, each country is a specific domain concerning the characteristics of SMES.

Prior studies Cheug et al. (2010) and Uyar (2011) have used total sales or the number of employees as a measurement of firm size (Kilic, Uyar& Ataman, 2016). In this study, total

assets, total liabilities, annual turnover and number of employees was used to determine the size of a firm, particularly number of employees (AABE, 2017).

#### **2.4. International Financial Reporting Standards (IFRS)**

IASB's Framework for the Preparation and Presentation of Financial Statements states that the objective use of financial statements is to present the wide range of users of these financial statements with information about the entity's financial position, performance and the changes in financial position. This helps in better equipping the users with more suitable economic decision making (Epstein & Jermakowicz, 2010). Initially, regulated financial statements were needed on country level in order to ensure that all the firms present their financial statements in a similar and consistent fashion. But the pace with which globalization is taking place, the need for internationally comparable financial reports were brought forward. Thus, in order to decrease the national differences and the differences in financial reporting, the international setters and regulators, for example, Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) have issued accounting standards such as Generally Accepted Accounting Standards (GAAP) and International Financial Reporting Standards (IFRS), respectively (Elliott B. & Elliott J., 2002).

IFRS, which is a principle based set of accounting standards, encompasses broad principles such as recognition principles, measurement principles, de-recognition principles, and presentation and disclosure principles. These principles are considered to be core elements of any set of accounting standards. These principles are derived on the basis of conceptual framework and are subject to professional judgment in their application in business scenarios (Nicoleta, Victoria, & Mariana, 2009). On the contrary, the US GAAP is more of rules based set of accounting standards, although both IFRS and GAAP almost share the same general principles and conceptual framework. Being principle-based IFRS provides fewer details in its standards as compared to GAAP. Majority of countries throughout the world today use IFRS for their financial reporting. IFRS serves to be an international financial language which can be easily and reasonably interpreted by the users of these financial statements (Elena, Catalina, Stefana, & Niculina, 2009).

## **2.5. International Financial Reporting Standard for Small and Medium Enterprises (IFRS for SMEs)**

According to International Accounting Standards Board (International Accounting Standards Board, 2010), the IFRS for SMEs is a self-contained standard designed to meet the needs and capabilities of small and medium-sized entities (SMEs), which are estimated to account for over 95% of all firms around the world. IFRS for SMEs is about good financial reporting made simple. It is simplified IFRSs, but built on an IFRS foundation. It is designed specifically for SMEs and is internationally recognized. The IASB took six years to develop it. The final standard was issued by the IASB on the 9th of July 2009. The standard is available for any jurisdiction to adopt, whether or not it has adopted full IFRSs. Each jurisdiction must determine which entities should use the standard. The IASB's only restriction is that listed firms and financial institutions should not use it. Over 99% of private entities around the world are expected to be eligible to use the standard. The definition is therefore based on the nature of an entity rather than on its size. Where a transaction is not addressed by the IFRS for SMEs, management is expected to use judgment to determine its accounting policy. If such a transaction is covered in full IFRS, management may refer to the appropriate international standard if it wishes but is not required to do so by the IFRS for SMEs (Pricewaterhouse Coopers, 2009).

## **2.6. Small and medium-size Enterprises (SMEs)**

Small and Medium Enterprises (SMEs) play a major role in most economies, particularly in developing countries. SMEs account for the majority of businesses worldwide and are important contributors to job creation and global economic development. They represent about 90% of businesses and more than 50% of employment worldwide (World Bank, 2019). Formal SMEs contribute up to 40% of national income (GDP) in emerging economies (World Bank, 2019). These numbers are significantly higher when informal SMEs are included. According to World Bank estimates, 600 million jobs will be needed by 2030 to absorb the growing global workforce, which makes SME development a high priority for many governments around the world. In emerging markets, most formal jobs are generated by SMEs, which create 7 out of 10 jobs (World Bank, 2019).

Different studies showed that countries are not using the same definition for small and medium-sized firms around the world. However, there are different ways to define SMEs; some factors are number of employees, balance sheet total, size and range of products, revenue, turnover, markets, and so on. The following section shows some definitions of SMEs.

According to Hallberg (2000) the majority of definitions or classifications of small businesses are specific to the context within which SMEs are defined or classified. The definitions vary across countries and regions and according to the size and structure of the economy.

According to IASB, Decisions on which entities are required or permitted to use the IFRS for SMEs Standard rest with the legislative and regulatory authorities and standard-setters in individual jurisdictions (paragraph 13 of the Preface to the IFRS for SMEs Standard). Many jurisdictions have developed their own definitions of SMEs for a broad range of purposes, including prescribing financial reporting obligations. Those national or regional definitions often include quantitative criteria based on revenue, assets, employees or other factors.

The term ‘small and medium-sized entities’ as used by the Board in the Standard is defined in the Glossary and is explained in paragraphs 1.2–1.7 of the Standard. The key element of an SME, as defined by the Board, is that it does not have public accountability (see paragraph 1.3) and that it publishes general purpose financial statements (as defined in the Glossary). The notes and examples to paragraphs 1.2–1.7 expand on these elements.

The Board’s definition of SMEs does not include quantified size criteria for defining a small or medium-sized entity because it is not feasible to develop quantified size tests that would be applicable and long-lasting in numerous jurisdictions.

As noted above, a country may choose to prescribe quantified size criteria in deciding which entities should be required or permitted to use the IFRS for SMEs Standard. However, an entity would still need to assess whether it complies with the definition of an SME in the Standard before concluding whether it can assert compliance with the Standard.

Similarly, a country may decide that it’s economically significant entities should be required to use full IFRS Standards rather than the IFRS for SMEs Standard. According to International Accounting Standard Board (IASB), the Small and Medium-Sized Entities (SME) can be

characterized into three categories; micro, small and medium-size enterprises. The basic requirements for Small and Medium-Sized Entities (SME) are 1) Firms do not have public accountability, 2) prepare general purpose financial statements for external users (IASB, 2010).

From above definition it is clear that, the entities which have public accountability are capital market oriented entities and entities that have assets for broad groups of outsiders in a fiduciary capacity, whether or not they are capital market oriented. Hence, SMEs are neither listed entities nor financial service business.

With regard to African countries, Sandy (2003) noted that there are diverse definitions of SMEs, and there is no regional or national consensus on the definition.

In Ethiopia, enterprises are categorized under small and medium enterprises based on total capital investment, number of employees, annual turnover, production capacity, total assets and two broad sector classifications industry and service as well as taking into account inflation and exchange rate related changes that might occur over the next five years. For industrial sector manufacturing, construction and mining, small enterprises are defined as enterprises with total assets from ETB 100,001 up to ETB 1,500,000 (USD 4,300 up to USD 69,500) and that employee 6-30 workers. For service sector (hotel, tourism, retail trade, and information technology and maintenance service), small enterprises are defined as enterprises with total assets of at least ETB 50,001 and up to ETB 500,000 (USD 2,310 up to USD 23,150). In similar manner, Medium enterprise is an enterprise which has more 30 employees & total assets more than 1,500,000 ETB for industrial sector and more than 500,000 ETB for service sector (MSEDPS, 2016).

Moreover, Federal Small and Medium Manufacturing Industry Development Agency defined small manufacturing industry as an industry having a total capital, excluding building, from ETB 100,001 up to ETB 1,500,000 in the manufacturing sector and engaged from 6 to 30 employees including the owner, his family members and other employees and medium manufacturing industry is defined as an industry having a total capital, excluding building, from ETB 1,500,001 to ETB 20,000,000 in the manufacturing sector and engaged from 31 to 100 employees including the owner, his family members and other employees (FesMMIDA, 2016).

## **2.7. Summary of literature and Research gap**

Previous studies on the adoption of IFRS for SMEs in different countries conducted by Albu (2013), Quagli & Paoloni (2012), Hussain, F., Chand, P., & Rani, P. (2012), Eierle & Haller (2009), Masca (2012) indicated that the adoption of IFRS for SMEs in Europe is influenced by accounting culture of the geographical area in which they operate.

According to Chand & White (2015) (cited in Sellami and Gafsi, 2018), several developing countries still face challenges in implementing IFRS for SMEs due to lack of adequate accounting training, limited professional capacities and high training costs that are major factor hindering the adoption and implementation of IFRS for SMEs. On the other hand, accountants and practioner in Big 4 firms have played a supporting role in properly implementing IFRS for SMEs in many past developers like Fiji because they have high quality training and sufficient expertise (Hussain et al., 2012). However, a study conducted by Kaya & Koch (2015) showed that there is no significant relationship between education level and the decision of adopting IFRS for SMEs. This shows that there is inconsistency of research results.

IFRS for SMEs too costly to apply and SMEs reporting entities are more concerned about the costs associated with conversion rather than the benefits obtained from using the standard (Hussain et al., 2012; Litjens, S., & Vergoossen, 2012). However, a study conducted by Albu et al. (2013) stated that stakeholders do not recognize the implementation of IFRS for SMEs as a cost burden rather considered it as an opportunity to make better the business environment by training accountants and disclosing a quality accounting information. This implies that the impact of conversion cost and IFRS for SMES adoption decisions are not consistent across different studies.

Several developed and developing countries have actually adopted IFRS for SMEs and others have plans to adopt the standard. The issue of benefits and challenges of adopting IFRS for SMEs in developed countries have already been studied, but very few studies have been conducted in developing countries in Africa, particularly in Ethiopia. Prior researches in Ethiopia have focused on the challenges or factors affecting the adoption of full IFRS (Arefainie, 2018; Hache, 2019; Alemgena, 2016; Fikru, 2012; Melese, 2016; Firdawek, 2017).

Despite the benefits it has, there are factors that affect IFRS for SMEs adoption decision. Out of the previous studies, most of them examined the challenges or factors affecting adoption of IFRS for SMEs as lack of awareness, lack of technical skills, high cost of implementation, education level, but few have tried to examine firm size (Panagiotidou, 2015; Chege et al., 2016; Mazhindu et al., 2013; Kuqi & Jonuzi, 2011). To the researcher knowledge, a report by Mukokoma & Tushabomwe-Kazooba (2019) is the only study prepared as a report that examined the firm size as mediation influence on the relationship between adoption decision and enablers and inhibitors. Moreover, there is no empirical research focusing on the effect of regulatory body enforcement strategy on SMEs decision to adopt IFRES for SMEs. Unlike previous studies, this study include factors such as enforcement strategy of regulatory body and the mediation influence of firm size between adoption influencing factors and SMEs adoption decision, to better examine them in the context of Ethiopian economy.

Even though IFRS for SMEs seems to be equally important for all countries, there is a no enough empirical study that examines the data from developing countries and in particular in SMEs in Ethiopia. The Various challenges reported by previous studies on the adoption of IFRS for SMEs vary by countries, so that cannot be generalized and generalizing of these challenges may not bring possible solution to specific country like Ethiopia. As far as the knowledge of the researcher is concerned, in the case of Ethiopia, the major factors of adopting IFRS across SMEs have not been clearly identified. It indicates that, the factors affecting the adoption of IFRS for SMEs in Ethiopia if any are still need to be assessed to successfully adopt IFRS for SMEs. Therefore, this study makes an attempt to bridge this gap and elaborate those factors that could influence the adoption of IFRS for SMEs in Ethiopia.

## **2.8. Conceptual Framework**

According to Kotler (2000), a conceptual framework is a basic structure that consists of certain abstract blocks which represent the observational, the experiential and the analytical/synthetically aspects of a process or system being conceived. The interconnection of these blocks completes the framework for certain expected outcomes. For the purposes of this research, the dependent variable is the adoption of IFRS for SME's while the independent variables are awareness of IFRS for SMEs, education qualification level and training, cost of conversion, role and enforcement strategy of regulatory body and firm size is a mediating factor.

This study considered SMEs owner managers and accountants as one of the important stakeholders that need to be aware of the standards for the adoption of IFRS for SMEs. Therefore, the conceptual framework for the study was based on the hypothesis that the adoption process of IFRS for SMEs can be examined through different factors from nature of the firm, accountants and managers point of view. For this research, the factors considered were awareness of IFRS for SMEs by managers and accountants, education level and training of managers and accountants, cost of conversion, enforcement strategy for proper adoption of IFRS for SMEs and size of the firm.

### Conceptual framework

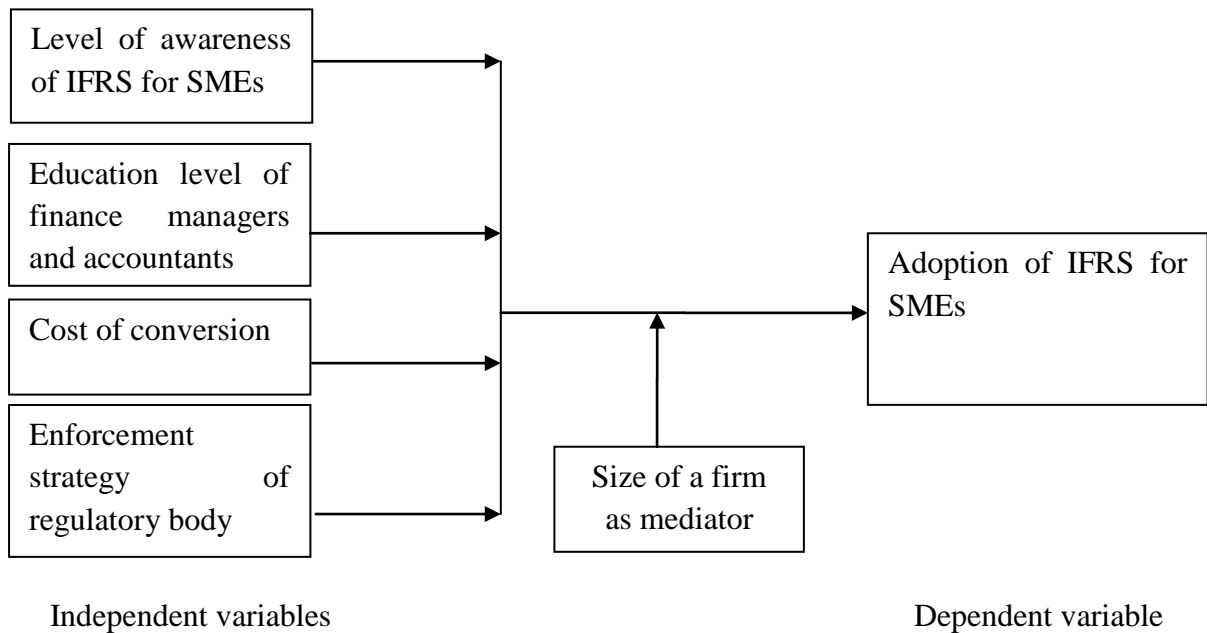


Figure 1: Conceptual framework of factors affecting adoption of IFRS for SMEs

Source: Mukokoma & Tushabomwe (2019), modified by the researcher

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1. Introduction**

This chapter presents the research methodology employed to address research questions of this study. The first part of the chapter provides an overall view of research approaches. Then, research design, sources of data collection, research instruments, target population, sample selection and method of data analysis for the study are outlined and linked with research questions.

#### **3.2. Research methods/approaches**

According to Creswell (2008), there are three types of research approaches, namely; quantitative research approach, qualitative research approach and mixed research approach. Quantitative research approach relies on numeric data in quantitative experiments and survey and collect data on a predetermined instrument that yield statistical data (Creswell, 2008). According to Charles and Mertler (2002), a researcher relies on numeric data in quantitative research. Quantitative research can employ large sample size; can test validity and reliability of instruments (Creswell, 2009). Quantitative research approach focuses mainly on construction of quantitative data that consists of numbers constructed by researcher using the process of measurement (Kent, 2007 cited in Ababaw, 2018).

According to Creswell (2008), qualitative research is a means for exploring and understanding the meaning individuals or groups ascribe to social or human problem. Collecting data under qualitative research framework through interview and observation provide greater insight on issues while conducting a study (Kato, 2002). Qualitative research is framed in terms of using words rather than numbers and using open-ended questions rather than closed ended question to collect data (Creswell, 2008). According to McDonald and Daly (1992), qualitative research approach is essential when the researcher(s) has (have) little knowledge about the area of the study.

According to Creswell and Clark (2011), mixed research approach follows pragmatic paradigm which serves in mixing of quantitative and qualitative approaches. It helps in triangulating evidence from quantitative and qualitative data. It involves the use of collecting and analyzing both quantitative and qualitative data and the overall strength of a study is greater than either quantitative or qualitative research approaches (Creswell, 2008).

Keeping the features of these approaches in mind, to collect sufficient data to answer the research questions and better understand the problem identified in the research, this study employed mixed research approach.

### **3.3. Research design**

According to Marczyk et al. (2005), choosing the most appropriate research design is very important to any researcher. The research design reflects the overall plan regarding the way of answering the research question (Saunders et al., 2009). It covers clear aims, resulting from the research question, determines the sources used to collect data, and deliberates the limitations that are inevitably faced. For instance, access, time, location and cost in addition to cover ethical matters (Saunders et al., 2009). In this study, the research purpose is considered as explanatory. It is explanatory because this study is concerned with cause-effect relationship. According to Yin (1994) the study can be explanatory explaining which causes produce which effects, when a study focuses on cause-effect relationship. The concern in this study is how the independent variables influence the dependent variable. In this study, the researcher is more interested in understanding, explaining, and predicting relationships between variables.

With regard to the time horizon, this study is considered as cross-sectional study as it is using the questionnaire survey to investigate the factors that influence the adoption of IFRS for SMEs at a particular time that corresponds to the period of this. “Cross-sectional design involves the collection of data on more than one case and at a single point in time in order to collect a body of quantitative or quantifiable data in connection with two or more variables, which are then examined to detect patterns of association” (Bryman& Bell, 2007).

In general, the study used a cross-sectional explanatory research design in order to answer the research questions.

### **3.4. Sources of research data collection**

The study collected primary and secondary data. Primary data provided a presentation of the actual information that was obtained to accomplish the objectives of the study. The primary data was gathered using self-completion questionnaire and semi-structured interviews. Secondary data such as empirical and theoretical literatures were sourced from books, journal and internet.

### **3.5. Research instruments**

Research instruments are tools used for collecting data needed to find solutions to the issues under investigation. Tools for data collection include questionnaires, interviews, participant observation, non-participant observation, and focus group discussions (Sekaran, 2000). For this study, the researcher used the questionnaires and interviews as research instruments.

#### **3.5.1. Semi-structured interview**

Among several types of interviews, semi-structured interview was chosen for this study. It provided “some flexibility to not only interviewers to reword or reorder the questions” (Johnson & Turner, 2003), but also interviewees to “explain their thoughts and to highlight areas of particular interest and expertise that they felt they had” (Horton, Macve, Struyven, 2004, p. 340).

Interviews was conducted with various groups; owner-managers, manager and accountants. Besides the researcher conducted interviews with some employees and official of AABE. Furthermore, an auditor was interviewed because of auditors close relationship with SMEs and good understanding in the adoption of the standard.

#### **3.5.2. Questionnaire Survey**

A questionnaire survey is viewed as “an efficient means of data collection when value, opinion, or belief is a subject of interest” (Robson, 2011). As compared to other survey methods, “cost and ease of implementation are major advantages of questionnaire survey; especially it allows a study of the perceptions of a large number of persons who are geographically dispersed” (Bryman & Bell, 2011). One of its disadvantages, however, is low response rate, and loss of opportunity to probe and correct misunderstanding of respondents (Oppenheim, 1992).

This study employed the paper-based questionnaire as a method of collecting data for the research. To some extent collecting data was difficult because of COVID-19 outbreak, so that the researcher used online survey method in addition to the paper-based questionnaire.

### **3.6. Target population**

The target population for the study consists of total registered SMEs in Addis Ababa. The criteria to decide a firm as SMEs is defined in the AABE roadmap for IFRS adoption as discussed in chapter two. Therefore, for this study the population size is the number of SMEs registered with Accounting and Auditing Board of Ethiopia (AABE) and 15, 300 registered SMEs are the target population and comprise all kinds of SMEs in Addis Ababa. The list and contact details of SMEs were obtained from AABE and Ministry of Trade.

### **3.7. Sample selection and size**

According to Bryman & Bell (2007), the representative part of the whole population is known as sample, and the appropriate selection of sample is crucial for the reliability of the research.

The selection of the sample was done through stratified random sampling whereby SMEs are grouped into manufacturing sector, service sector, construction sector, retail trade and real estate. The researcher also selected respondents from auditors. Auditors were considered as samples because they work closely with the SMEs and provide them with different kind of accounting, auditing and consulting services.

Based on sample size determination random tables by Sekaran (2003, pp 294), a maximum number of three hundred seventy five SMEs appropriate for the study. Based on the database obtained from the sources mentioned above three hundred seventy five SMEs selected at random and questionnaires were distributed, out of which two hundred thirty two questionnaires were collected and used for analysis.

The following number of SMEs owner-manager, manager, accountant and auditors was used for the interviews:

Category	Total number
SMEs	4
Auditors	1
AABE employee	2
Total	7

Convenient sampling technique was used in selecting auditors and the managers, or accountants of SMEs selected for the study.

To collect data using questionnaire from respondents, Five points Likert scale of SA=Strongly Agree, A=Agree, N=Neutral, DA=Disagree and SD=Strongly Disagree was used.

### 3.8. Regression Analysis Model of the Study

The researcher used the following binary logistic regression model to test the research hypothesizes. The researcher motivated to use the binomial logistic regression model in view of the fact that the dependent variable is a dichotomous variable and several studies used the model on adoption of IFRS for SMEs (Kaya and Koch, 2015; Zeghal & Mhedhbi, 2006; Zehri & Chouaibi, 2013; Pais, 2018).

$$P(\text{IFRS-sme}_i) = \beta_0 + \beta_1 \text{EDUC} + \beta_2 \text{COSIMP} + \beta_3 \text{RENFRS} + \beta_4 \text{AWARN} + \beta_5 \text{SIZEFR} + \varepsilon_i$$

Where:

IFRS-sme <sub>i</sub>	Adoption of IFRS for SMEs	Dummy variable were assigned to the respondents' response on adoption progress level
AWARN	Awareness of IFRS for SMEs	Dummy variable were assigned to the respondents Preference of opinion on awareness
EDUC	Education and training	Dummy variable were assigned to the respondents Preference of opinion on education and training
COSCON	cost of conversion	Dummy variable were assigned to the respondents Preference of opinion on cost of adoption
RENFRS	Role and enforcement strategy	Dummy variable were assigned to the respondents Preference of opinion on role and enforcement Strategy of regulatory body
SIZFR	Size of the firm	Dummy variable was assigned to the category of number of employees

### 3.9. Measurement of Variables

Regarding the dependent variable IFRS for SMEs, considerable information on the adoption process by a firm include:

- 1) Adopted – a firm that has already assessed the impact of IFRS for SMEs on its accounting system trained its staff and converts its accounting system in accordance with IFRS for SMEs;
- 2) In progress- a firm that has initiated move to convert to IFRS by providing training for employees, making some changes to its accounting information processing system, and other procedures but not fully convert IFRS for SMEs;
- 3) Not ready to adopt yet- a firm that has not initiated moves to convert to IFRS for SMEs.

Based on this view, the IFRS for SMEs adoption decision was measured by requiring respondents to state the adoption progress of the standard in their firm as; adopted, in progress and not ready to adopt yet.

The research independent variables; awareness, education and training, cost of conversion, role and enforcement strategy were measured using items adapted from previously used scales in different researches and researcher's own developed items. Five- point Likert scales ranging from “strongly disagree” to “strongly agree” were used to measure the items. Five items were used to measure each independent variable. The size of the firm was measured by number of employees.

For further inferential statistical analysis, the variables were measured as follows;

IFRS for SMEs adoption decision - Assigned a binary variable (dichotomous variable), which has a value one, if the firm adopted IFRS for SMEs standard, zero otherwise.

Education and training (EDUC) - Derived by finding the median score of items measuring education and training and assigning dummy variable to the respondent's preference of opinion on education & training.

Awareness IFRS for SMEs (AWARN) - Derived by finding the median score of items measuring awareness and assigning dummy variable to the respondent's preference of opinion on awareness of IFRS for SMEs

Cost of conversion (COSCN)-Derived by finding the median score of items measuring cost of conversion and assigning dummy variable to the respondent's preference of opinion on cost of conversion.

Role and enforcement strategy (RENFRS) - Derived by finding the median score of items measuring role and enforcement strategy and assigning dummy variable to the respondent's preference of opinion on role and enforcement strategy.

Size of the firm (SIZFR) - Dummy variable assigned to the number of employees category

### **3.10. Data collection procedure**

Data collection was conducted in two phases:1) pilot study 2) the main study. In the pilot study, SMEs were randomly selected to pretest the questionnaires and the questionnaires were administered to twenty two SMEs in Addis Ababa. Interviews were also conducted with two auditors and one professional accountant to provide a comment on the contents of the questionnaire. Based on the response from these SMEs minor modifications were made to the questionnaire for the main phase of data collection. In the main study phase, questionnaires were distributed to three hundred seventy five SMEs in Addis Ababa.

The questionnaire required respondents' view whether their firm adopted IFRS for SMEs or adoption is in progress or not ready to adopt the standard yet. The questionnaire also required respondents to give their preference of opinion on five-point Likert scale questions the extent to which they "Disagreed" or "Agreed with IFRS for SMEs adoption and adoption challenge factors.

The responses to the questionnaire were coded as follows;

Strongly Disagree (SD)	1 point
Disagree (D)	2 points
Undecided (U)	3 points

Agree (A)	4 points
Strongly Agree (SA)	5 points

### 3.11. Reliability of Instrument

The internal consistency or reliability of items in the questionnaire was assessed using Cronbach's alpha coefficient.

Table 2 Reliability Test (Cronbach's Alpha)

Variable	No. of items	Cronbach Alpha
Company's awareness of IFRS for SMEs	3	.8387
IFRS for SMEs conversion cost	4	.8524
Education level and training	5	.8496
Role and enforcement strategy of regulatory body	4	.9174
overall Cronbach's alpha result	16	0.82

Source: Survey data, 2020

Table 2 above shows the result of the reliability test estimated using 22 questionnaires which includes 16 items in each questionnaire. The internal consistency or reliability of the instrument was assessed using Cronbach's alpha coefficient. According to Sekaran (2006), the acceptable values for the Cronbach's alpha reliability should be more than .6(60%) or more than .7(70%) in other sources. As shown in the above table, all Cronbach's alpha coefficients were above the cutoff recommended by the sources, showing that the research instrument is reliable and the researcher can apply different statistical tests and can interpret the results. The overall Cronbach's alpha result showed 0.82.

### 3.12. Construct Validity

The relationship between items relating to each other measuring similar variable was examined using factor analysis as follows:

Table 3 Component matrix of Awareness of IFRS for SMEs

Awareness of IFRS for SMEs statements	score
Organization's accounting staff lacks adequate information about the key difference between GAAP, FULL IFRS and IFRS for SMEs.	0.835
Organization's accounting staff has a limited or no understanding of IFRS for SMEs adoption and implementation process.	0.823
In your Organization little is known about the benefits of adopting IFRS for SMEs	0.657

Source: Survey data, 2020

Table 4 Component matrix of education and training

Education and training statements	Score
IFRS for SMEs adoption requires a high level of education & well skilled accounting professionals	0.753
Low level qualification of accounting education is obstacle for the adoption of IFRS for SMEs	0.766
Lack of adequate technical capacity for conversion process is a challenge for successful adoption of IFRS for SMEs	0.897
There was no adequate practical training on IFRS for SMEs conversion process prior to its adoption	0.663
Unavailability of training facilities and training center is obstacle to get accountants trained on IFRS for SMEs	0.561

Source: Survey data, 2020

Table 5 Component matrix of cost of conversion

Cost of conversion statements	Score
Cost of hiring external consultant or advisor for assisting adoption of IFRS for SMEs is high.	0.663
Cost of staff training and development is high.	0.702
Cost of changing or upgrading accounting information system or IT is high.	0.854
The other operating costs, beyond those identified in the questionnaire, associated with adopting IFRS for SMEs could be significant.	0.433

Source: Survey data, 2020

Table 6 Component matrix of role and enforcement strategy of regulatory body

Role and enforcement strategy statement	Score
Little or no effort was being made by regulatory body to encourage adoption of IFRS for SMEs	0.897
There is no effective practice review, and monitoring mechanisms that ensure proper and effective adoption and implementation of IFRS for SMEs roadmap	0.815
There is lack of technical guidelines, interpretations and other supporting materials in Ethiopian context that assist the successful adoption of IFRS for SMES.	0.897
Absence of adequate workshops, seminars, forums to be organized by responsible body impacts the successful adoption of IFRS for SMEs	0.842

Source: Survey data, 2020

According to Nunnally (1978), factor loading above 0.5 are acceptable. All the rotated factor loading except one as shown on the above tables are above 0.5.

Here, the items related to each other measuring the same element were combined into single variable known as composite research variable. A score for composite research variable was the median of the respondent's scores for each item. A score for composite research variable was used for inferential statistical analysis.

### 3.13. Methods of Data Analysis

Data collected using the questionnaires instrument for the hypothesis was analyzed using STATA version 14.2 software packages. Analysis was performed using descriptive statistics and inferential statistics. Descriptive statistics was used to measure the level of adoption of IFRS for SMEs by SMEs and demographic characteristics of respondents. Inferential statistics was performed using binary logistic regression to test the research hypothesis. The data that was collected using interview instrument were qualitatively analyzed and the narrative approaches of analyzing the data including quotations from respondents were used.

## CHAPTER FOUR

### DATA PRESENTATIONS, ANALYSIS AND DISCUSSIONS

#### 4.1. Introduction

This chapter presents the analysis of data collected from respondents about factors affecting the adoption of IFRS for SMEs by SMEs. The researcher distributed questionnaires to randomly selected respondents of retail trade, service, construction, real estate and manufacturing SMEs in Addis Ababa. A total of three hundred seventy five questionnaires were administered of which two hundred thirty two were returned and used for analysis.

#### 4.2. Data Presentation

##### 4.2.1. Demographic features of respondents

Demographic features of respondents and results of the analysis showing their gender, work experience, education level and position in the organization were presented in table 1 below.

Table 7 Demographic features of respondents

Variable		frequency	percent
Gender	Male	132	61%
	Female	83	39%
Length of work experience	Below 5 years	24	11%
	6-10 years	86	40%
	11-15 years	70	33%
	Above 15 years	35	16%
Education level	High school	0	0%
	TVET Diploma	55	26%
	Bachelor Degree	122	57%
	Master	38	18%
Job title	Owner-manger	19	9%
	Manager	56	26%
	Accountant	138	64%
	Budget revenue head	2	1%

Source: Survey data, 2020

The result in table 7 above shows, the proportion of male respondents was 61% and female respondents were 39%. 89% of the respondents' had a minimum work experience of 6 years and above. With regard to education, above 26% diploma holders, 57% bachelor degree holders, and

17% master degree holders. As shown in the table 7 above, the minimum level of respondents' education was diploma. The analysis of the current position or job title of the respondents in the organization shows that 10% in the owner-manager position, 25% in the manager position, 1% in the budget revenue head position, and 64% were in the accountant position. The data on the education level, job title and length of work experience of the respondents suggests that respondents are in good position to understand and provide the answers to the research questions.

#### 4.2.2. Descriptive statistics on IFRS for SMES adoption level

Table 8 IFRS for SMES adoption level

Adoption status	Frequency	Percent
Not ready to adopt	125	58%
In progress	61	29%
Adopt	29	13%
Total	215	100

Source: Survey data, 2020

As shown in table 8 above, the IFRS for SMEs adoption status was given in terms of those firms that have adopted, those firms that are In progress- firms that have initiated move to convert to IFRS for SMEs and those firms that have Not ready to adopt yet- firms that have not initiated moves to convert to IFRS for SMEs. The results of the data analysis indicates that 13% % of the firms had adopted IFRS for SMEs, 29% in progress to adopt the standard and 58% had not ready to adopt IFRS for SMEs. The result indicates that the adopted level is very low. Afterward, the researcher used the information to re-classify the adoption level into two categories, adopted and not adopted. Firms that were categorized under in-progress had in real meaning not adopted the IFRS for SMEs standard. Therefore, the data analysis result indicates that 87% of firms had not adopted the standard.

Previous studies findings such as Mazhindu et al., (2013) in Zimbabwe showed that 80% of SMEs did not maintain accounting records and had not adopted IFRS for SMEs. The finding of the study by Arthin et al., (2017) in Ghana concludes that IFRS for SMEs adoption and implementation in the Kumasi Metropolis is terribly very low. The finding of the study conducted by Mukokoma & Tushabomwe (2019) in Uganda concluded that 89% of firms had not dully adopted the standard. However, the findings of Rudzani et al., (2016) showed 67% of

SMEs in South Africa have adopted and implemented IFRS for SMEs, even though the challenges for doing so are huge.

Therefore, the researcher concluded that adoption and implementation of IFRS for SMEs in Ethiopia is very low like other developing countries.

#### 4.2.3. Descriptive statistics to answer research questions

This study examines the factors affecting adoption of International Financial Reporting Standard for Small and Medium Enterprises in Addis Ababa, Ethiopia. The factors include awareness of IFRS for SMEs, education level and training, cost of conversion, role and enforcement strategy of regulatory body and size of firm as mediation influence. The researcher used questionnaires to analyze it and the overall mean of the score are used for the analysis. Accordingly, the overall mean score between 4.20-5.00 is considered as strongly agreed (SA), score between 3.40-4.19 means respondents agreed (A), score between 2.60-3.39 is considered as undecided (U) opinion of the respondents, score between 1.8-2.59 shows respondents disagreed opinion and score between 1-1.79 shows that respondents are strongly disagreed on the issue.

##### 4.2.3.1. Research question 1

To what extent company's awareness of IFRS for SMEs affects SMEs adoption decision in Ethiopia?

Table 9 Descriptive statistics: To what extent company's awareness of IFRS for SMEs affects SMEs adoption decision in Ethiopia?

Awareness of IFRS for SMEs	Mean	SD	
Lack of adequate information about the key difference between GAAP, full IFRS and IFRS for SMEs affects the decision to adopt IFRS for SMEs.	3.82	1.24	Agree
Limited or no understanding of IFRS for SMEs adoption and conversion process affects the decision to adopt IFRS for SMEs.	3.86	1.21	Agree
Little or no understanding of the importance of adopting IFRS for SMEs affects the decision to adopt IFRS for SMEs.	4.03	.91	Agree
Overall	3.90		

Source: Survey data, 2020

This section describes the respondents' opinion about the influencing factor of lack of awareness of IFRS for SMEs on the decision to adopt the standard by SMEs in Addis Ababa. Lack of awareness of the standard was assessed in terms of lack of adequate information about the key

difference between GAAP and IFRS for SMEs, limited or no understanding of IFRS for SMEs conversion process, and little understanding of the importance of adopting IFRS for SMEs by small and medium enterprise in Addis Ababa, Ethiopia. The mean responses for each statement are shown in table 9 above, and the overall mean result was 3.90. This indicates that respondents agreed lack of awareness of IFRS for SMEs influences the decision of SMEs in Addis Ababa, whether or not to adopt the standard. The lack of adequate information about the key difference between GAAP and IFRS for SMEs, limited or no understanding of IFRS for SMEs adoption and conversion process, and little or no understanding of the importance of adopting will challenge majority of small and medium enterprises in Ethiopia to adopt IFRS for SMEs.

This result is consistent with the findings of the study conducted in Nigeria by Isenmilla & Adeyemo (2013 a); Tude (2017) as lack of awareness about adoption of IFRS standards make required firms not ready to adopt it.

On the issues of awareness of IFRS for SMEs, interviewee owner-manager of a firm that has not adopted IFRS for SMEs highlighted having no familiarity with IFRS for SMEs and the major factor that influence the adoption process is lack of awareness; and said; “I don’t understand IFRS for SMEs and even the benefits of implementing International Financial Reporting Standard”. “In our organization, none of the employees understand the international financial reporting standard in view of the fact that exposure to the concept of IFRS was recent in Ethiopia. It is one reason for lack of preparedness to adopt it”. An accountant of a firm categorized under SME that has in progress to adopt IFRS for SMEs said; “I have little understanding about the theoretical concept of IFRS but not the application mechanism of IFRS for SMEs yet”. Moreover, Interviewee said:” I don’t have adequate information about the key difference between IFRS for SMEs, full IFRS and US GAAP because the theoretical training I have taken mainly focuses on IFRS in general. There is low level of awareness among practioners; some of them are not fully aware of the practical implementation of IFRS for SMEs”.

#### **4.2.3.2. Research question 2**

What impact or aid does education level and training have on IFRS for SMEs adoption decision?

Table 10 Descriptive statistics: what impact or aid does education level and training have on IFRS for SMEs adoption decision?

Education level and training	Mean	SD	
IFRS for SMEs adoption requires a high level of education & well skilled accounting professionals	3.72	1.26	Agree
Absence of qualified accountant in the area of IFRS is obstacle for the adoption of IFRS by SMEs	3.67	1.21	Agree
Lack of adequate technical capacity for conversion process is a challenge for successful adoption of IFRS for SMEs	3.70	.92	Agree
There was no adequate practical training on IFRS for SMEs conversion process prior to its adoption	3.62	1.25	Agree
Unavailability of adequate training facilities and training center is obstacle to get accountants trained on IFRS for SMEs	3.63	1.24	Agree
Overall	3.67		

Source: Survey data, 2020

On the issue of education and training, to examine the respondents' level of agreement about the lack of accounting education and practical training, the researcher used five statements which judged their opinion whether or not lack of accounting education and practical training influences small and medium enterprises decision to adopt IFRS for SMEs. The mean responses for each statement are shown in table 10 above, and the overall mean result was 3.67. This indicates that respondents agreed lack of accounting education and practical training influences the adoption decision of the standard in the SMEs sector. Respondents agreed that to easily understand and interpret the contents of IFRS for SMEs, the standard requires high level of education and well skilled accounting professionals. Respondents agreed that low level of qualification of education in SMEs sector and lack of adequate technical capacity for conversion process contributes to the low adoption rate of the standard in Addis Ababa, Ethiopia. Respondents also agreed that lack of adequate practical training on conversion process and unavailability of training facilities and limited training centers are major influencing factors in the decision whether or not to adopt the standard.

Like previous studies Irvine and Lucas (2006), Judge, Li., & Pinsker (2010) and Zeghal & Mhedhbi (2016), who believes education level is the major factor for the decision to adopt IFRS, the finding of this study shows a significant relationship between education level and adoption of

IFRS for SMEs, but inconsistent with Yosra & Yosra (2018), and Kaya and Koch (2015) study findings.

Similarly, on the issues of education and training, an interview with owner manager of a firm indicates the concern for not having qualified staff to implement IFRS for SMEs. High education level is important for accountants to easily interpret and understand the standard and said; “Training is important for all employees of the company as the standard is a new experience in our country. The decision to adopt IFRS for SMEs requires the firm qualified accounting staffs with adequate knowledge on IFRS for SMEs, which the firm can’t hire from the environment. As a result adoption did not take place yet. Another interviewee, an auditor in Addis Ababa stated that absence of qualified accounting staff with knowledge of IFRS for SMEs is one of the major challenges SMEs face and said: “Most accountants available in the market are not qualified in terms of IFRS for SMEs, so that SMEs may faces a challenge in hiring such employees yet.”

Accountants and owner manager of a firm in SMEs category highlighted that training about IFRS for SMEs is important for employees of SMEs in order to easily familiar with the standard, but did not happen as expected: “The available trainings are group trainings. They do not include any practical activities. What are offered by training organizers right now are PowerPoint lectures that give only a general idea about the standard which is not useful for accountants. Accountants need practical training on the application mechanism of the standard.”

#### 4.2.3.3. Research question 3

To what extent that IFRS for SMEs conversion cost affects adoption decision by SMEs in Ethiopia?

Table 11 Descriptive statistics: To what extent that IFRS for SMEs conversion cost affects adoption decision by SMEs in Ethiopia?

IFRS for SMEs conversion cost	Mean	SD	
Cost of hiring external consultant or advisor for assisting adoption of IFRS for SMEs is high.	3.54	1.12	Agree
Cost of staff training and development is high.	3.59	1.30	Agree
Cost of changing or upgrading accounting information system or IT is high.	3.70	.93	Agree
The other operating costs, beyond those identified in the questionnaire, associated with adopting IFRS for SMEs could be significant.	3.66	1.13	Agree
Overall	3.62	1.15	

Source: Survey data, 2020

This section describes the respondents' opinion about the impact of high cost of conversion on IFRS for SMEs adoption decision. Cost of conversion was assessed in terms of cost of hiring external consultant or advisor for assisting adoption of IFRS for SMEs is high, cost of staff training and development is high, cost of changing or upgrading accounting information system or IT is high, and the other operating costs beyond those identified in the questionnaire associated with adopting IFRS for SMEs could be significant for SMEs. The mean responses of each statement are shown in the table 11 above, and the overall mean was 3.62. This indicates that respondents agreed high cost of conversion process influences the decision whether or not to adopt the standard by small and medium enterprises in Addis Ababa, Ethiopia. The overall mean result also indicates that respondents perceive cost of IFRS for SMEs conversion is high. This means that, SMEs in Addis Ababa encountered a problem of high cost of conversion to adopt IFRS for SMEs.

The finding that adopting IFRS for SMEs is influenced by high cost of conversion agrees with the findings of Mukokuma & Tushabomwe, (2019) in Uganda; Rudzani et al., (2016) South Africa, Jones and Higgins (2006) in Ghana, De George Ferguson, & Spear (2012), and Uwadiae (2012).

It is known that when firms adopt something that does not already exist, it brings certain costs in terms of human resource, physical resource and time. Some previous studies Jones and Higgins (2006), De George Ferguson, & Spear (2012), noted that some SMEs incurred high costs during the first time of their IFRS for SMEs adoption. SMEs in Ethiopia are not exception to this. During an interview, one accountant explained high cost of adopting IFRS for SMEs: "A decision to adopt IFRS for SMEs caused an increase in cost of hiring external consultant and high fees for staff training."

Owner-manager of a small firm highlighted the high cost of conversion of IFRS for SMEs harm their decision to adopt the standard. He explained: "one consultant proposed for us a high cost of consultant's fee which might not be affordable by the firm; as a result, we are not ready to adopt the standard". Another Interviewee highlighted that high cost associated with consultation fee and attending IFRS for SMEs training sessions is one of the challenges SMEs face: "The offered training from AABE and other trainers are more of theoretical and expensive for SMEs firms."

An accountant of a firm that had not adopted IFRS for SMEs also said: “we don’t know the amount of cost of conversion of the standard, as the adoption and implementation didn’t happen yet in our organization”.

#### 4.2.3.4. Research question 4

What is the likelihood that role and enforcement strategy of regulatory body affects the IFRS for SMEs adoption decision?

Table 12 Descriptive statistics: What is the likelihood that role and enforcement strategy of regulatory body affects the IFRS for SMEs adoption decision?

Role and enforcement strategy of regulatory body	Mean	SD	
Little or no effort was being made by regulatory body to encourage adoption of IFRS for SMEs	3.78	1.22	Agree
There is no effective practice review and supervision mechanisms that ensure proper and effective adoption and implementation of IFRS for SMEs roadmap	3.78	1.25	Agree
There is lack of technical guidelines, interpretations and other supporting materials in Ethiopian context that assist the successful adoption and implementation of IFRS for SMES.	3.90	1.23	Agree
Lack of adequate workshops, seminars, forums etc. is barrier for smooth transition & successful adoption of IFRS for SMEs	3.78	.93	Agree
Overall	3.81		

Source: Survey data, 2020

To gather opinions whether or not weak role and enforcement strategy of regulatory body influences SMEs decision to adopt IFRS for SMEs, the respondents were provided with four statements. The mean responses of each statement are shown in table 12 above, and the overall mean result was 3.81. The result indicates that the weak role and enforcement strategy of the regulatory body contributes for the low adoption rate of IFRS for SMEs in Addis Ababa, Ethiopia. This indicates that since the standard is a new concept in Ethiopia and majority of SMEs required to adopt the standard do not understand the importance of adopting IFRS for SMEs, SMEs sector requires encouragement, effective practice review and monitoring mechanism to enforce them to adopt the standard in accordance with the road map.

Respondents’ also agreed that there is lack of technical guidelines, interpretations and other supporting materials in Ethiopian context that assist the successful adoption and implementation of IFRS for SMES and lack of adequate workshops, seminars, forums etc. is barrier for smooth transition & successful adoption of IFRS for SMEs. As a result, majority of the required firms do

not understand the standard well and its adoption process which contributes for the low adoption rate in the country.

The result of this study agrees with Arhin et al. (2017) in Ghana, and John Kwaku, Siaw, & Mensah (2019) in Ghana that regulatory and professional bodies play weak role in regulating & enforcing and do not support SMEs to adopt the standard successfully. The result of the findings also consistent with Iyoha and Faboyede (2011);Ebogbue, (2016) findings in Nigeria who pointed out that the adoption of IFRS is influenced by a number of factors, which include among others professional support and government policies mechanisms towards encouraging organization to adopt IFRS. IFRS for SMEs adoption in Ethiopia will be implemented successfully when properly supported by good government policies and regulatory body positive enforcement mechanisms.

Interviews with some managers and accountants indicated that government and regulatory body should play great role to bring IFRS for SMEs adoption in to effect. Interviewee , owner-manager thought that “it is the responsibility of the government of Ethiopia to educate the citizen and help SMEs to adopt the standard since it is a new experience for Ethiopia to adopt the standard.” One auditor said: “government of Ethiopia should provide financial support to cover conversion and training costs or find mechanisms for the availability of training and conversion process with affordable price.” Two accountants also highlighted the other support SMEs need from the government and regulatory body AABE is to raise the awareness level of people and said” the government is the one that have the capacity to mobilize resources and organize workshops, seminars and trainings to raise people’s awareness. However, the government did not raise the required level of awareness about the standard.”

Moreover, the Interviewees highlighted in their opinion the extent to which SMEs need assistant from the government and regulatory body and said:” AABE should provide a team to answer questions raised form SMEs while adopting the standard. AABE should organize training courses in both Amharic and English languages. It has to prepare manuals that explain the difference between GAAP and International Financial Reporting Standard in a way easily understood by SMEs.”

AABE is the regulatory body responsible for implementation of full IFRS, IFRS for SMEs and IPSAS by any business type or size in Ethiopia. However, one officer highlighted that: “one major problem is no professional body or agency that assists SMEs to implement IFRS for SMEs. Because the number of SMEs is large, it is difficult to monitor all SMEs and provide guidance to all of them”. One official highlighted the way AABE handled the adoption process and said: “AABE announced the transition process on time. It coordinated with Ministry of Revenue to enforce SMEs to register for the adoption of the standard. AABE gave SMEs an additional one year time for preparation after the obligation date. It announced workshops to train practitioners in SMEs sector to raise their level of awareness about the standard”.

Moreover, an officer explains as they are not properly reviewing the adoption and implementation process. He said; “we are not monitoring and reviewing the adoption and implementation process of International Financial Reporting Standard. We need intensive practical training, workshops and seminars with regard to the review and monitoring mechanisms”.

#### 4.2.3.5. Research question 5

What significant role does firm size play in the relationship between adoption decision and adoption challenge factors?

Table 13 IFRS for SMEs general adoption status based on firm size

Number of employees	Adopted	In progress	Not ready to adopt	Total
<30	1	38	117	156
30-100	28	32	16	76
Total	29	70	133	232

Source: Survey data, 2020

Information in table 13 above indicates questionnaire data analysis of firm size in the context of adoption status. The result showed that most firms that have adopted the standard have more than 30 employees, they are comparatively medium organizations. The researcher therefore concluded that size of a firm affects the decision whether or not to adopt the standard.

The finding of the study consistent with previous studies of Leuz (2010) indicating that the larger the firm size, the more it likely to adopt the standard and the smaller the size of the firm, the less tendency it has to adopt the standard. It also consistent with a report of Mukokoma & Tushabomwe (2019), indicating that the adoption of the standard affected by the size of the firm. However, the result of this study is inconsistent with the findings of Eierle& Haller (2009).

With regard to firm size, Interviewees highlighted that not all firms equally responds to the adoption of IFRS for SMEs because of their size. Interviewed one owner-manager and an auditor said:”small firms may resist adopting the standard because most of them don’t hire qualified accounting staff rather they prefer to rely on external accounting consultant for the preparation of annual financial statements.

### **4.3. Results of logistic regression analysis to test research hypothesis**

For this study, factors influencing the adoption of IFRS for SMEs by SMEs are examined based on awareness, education and training, role and enforcement strategy of regulatory body, cost of conversion and size of firm. These factors are investigated using binary logistic regression analysis.

The researcher used binary logistic regression model based on the following three major reasons; first, the model has been adopted by many studies on adoption of IFRS for SMEs, such as; Zeghal & Mhedhbi (2006), Ana & Claudio (2018). Second, the dependent variable is dichotomous variable that takes the value 1 if the firm adopts the standard, otherwise 0. Since dichotomous dependent variables cannot predict a numeric value, they violate assumptions such as normality, homoscedasticity, and linearity. Therefore, the best fit method of controlling the sum of squared distance is inefficient if ordinary least squares (OLS) estimations is used. In order to avoid the inefficient parameter estimates using OLS, the maximum likelihood estimation (MLE), which maximizes the log-likelihood, is applied in the logistic regression to estimate the regression coefficient. Third, the logistic regression model can be expressed in the logarithm of the odds ratio, also known as the log-odds ratio, representing the linear function of the explanatory variables. This form of expression provides a more simplistic description of the probabilistic relationship between the independent variables and the outcome.

### 4.3.1. Diagnostic of Goodness-of-fit test

For correct results of the logistic regression, the goodness-of-fit test was done to test whether the estimated model fit the data well. If the model fits the data well, it fits the logistic regression assumptions. For this study, the researcher uses the Nagelkerke  $R^2$  test. As it is shown on table 15, the value of  $R^2$  is 0.40, indicating that the independent variables in the model are explaining 40% variation on the dependent variables. Therefore, the researcher can understand that the model of the study is providing a good fit to the data, indicating that the independent variables in this study are the major influencing factors of IFRS for SMEs adoption decision.

### 4.3.2. Diagnostic of Multicollinearity test

Table 14 Pearson correlation coefficient test

	IFRSsmes	AWARN	EDUC	COSCON	RENFRS
IFRSsmes	1.0000				
AWARN	0.1609	1.0000			
EDUC	0.1746	-0.0752	1.0000		
COSCON	-0.4569	-0.0394	-0.1150	1.0000	
RENFRS	0.1581	-0.0192	0.1344	0.0665	1.0000

Source: Survey data, 2020

According to Harrell (2015), multicollinearity test assists to identify outliers in logistic regression. Based on this view, the independent variables were tested for multicollinearity and outliers to conform if the data were suitable for a logistic regression model. For this study, the multicollinearity problem was examined through correlation analysis and collinearity tests.

The correlation matrix based on Pearson correlation coefficient test determines the degree of correlation between pairs of independent variables. The result in table 14, showed moderate and low correlation,  $r < 0.8$  indicating that the independent variables achieved the condition of Pearson correlation test.

Table 15 Collinearity test Tolerance and Variance Inflation Factor (VIF)

model		Collinearity result	
		Tolerance	VIF
1	AWARN	0.992	1.01
	EDUC	0.960	1.04
	COSCON	0.977	1.02
	RENFRS	0.975	1.03

Dependent variable is adoption of IFRS for SMEs (IFRS\_SMEs)

Source: Survey data, 2020

For this study, the multicollinearity problem also examined using collinearity test namely Tolerance and Variance Inflation Factor (VIF). According to Simonoff & Chatterjee (2013), an independent variable has high linear correlation with other independent variable if tolerance value is low or VIF has higher value. According to Allison (1999), there is no strict cutoff for tolerance, but less than .40 causes a concern, and a VIF above 10 is considered high degree of collinearity problem (Hair, Black, Babin, Anderson, & Tatham, 2006). The result in the table 15 showed that all VIF are less than 10 indicating the independent variables achieved the condition of multicollinearity.

### 4.3.3. Result of main analysis of logistic regression

Main analysis of econometric model:

$$P(\text{IFRS}_{\text{SME}_i}) = \beta_0 + \beta_1 \text{AWARN} + \beta_2 \text{EDUC} + \beta_3 \text{COSCON} + \beta_4 \text{RENFRS} + \varepsilon_i$$

Table 16 Logistic regression result of the model1

Variables	Prediction	Coefficient $\beta$	Significant level (p-value)
AWARN	+	2.729	0.013
EDUC	+	2.576	0.020
COSCON	-	-3.175	0.000
RENFRS	+	2.932	0.008
Dependent variable: adoption level of IFRS for SMEs (IFRS_SMEs)			
Sample size 232			
R2 of Nagelkerke 0.40			

Source: Survey data, 2020

#### 4.3.3.1. Awareness of IFRS for SMEs

The result in table 16 above, show a positive and significant coefficient, at 5% level, AWARN, on the decision to adopt IFRS for SMEs. This shows that there is significant relationship between IFRS for SMEs awareness and decision to adopt the standard. This means IFRS for SMEs awareness affects the decision to adopt IFRS for SMEs. Thus, SMEs necessarily base on awareness of IFRS for SMEs to decide whether to adopt or not. Therefore, based on the result the researcher rejects the null hypothesis. The result of the present study is consistent with previous studies conducted by Uyar and Gungormus (2013), Kılıç, Uyar and Ataman (2014) and

Arhin, Perprem, & Hulede (2017). For example; because of the complexities of the standards, SMEs in Turkey were unaware of the key differences between full IFRS and IFRS for SMEs. According to Fortuin (2011), the relationship between adopting IFRS for SMEs and its benefits is not known by many businesses. This is an indication that SMEs lack awareness of the benefit obtained from adopting the standard that may affect businesses from adopting IFRS for SMEs.

Similarly, interviews results can be generalized as lack of awareness about IFRS for SMEs influences the adoption of IFRS for SMEs in small and medium enterprises sector in Addis Ababa, Ethiopia.

#### **4.3.3.2. Education and training**

Logistic regression result Table 16, shows a significant positive relationship between IFRS adoption and education level and training, with a regression coefficient of 2.053, and P-value of 0.017 and indicates that education level and training significantly predicts the adoption of IFRS for SMEs. Thus, SMEs necessarily base on education level and particularity on practical training to decide whether to adopt or not. Therefore, based on the result the researcher rejects the null hypothesis. Like previous studies Irvine and Lucas (2006), Judge, Li., & Pinsker (2010) and Zeghal & Mhedhbi (2016), who believes education level is the major factor for the decision to adopt IFRS, the finding of this study shows a significant education level and adoption of IFRS for SMEs, but inconsistent with Yosra & Yosra (2018), and Kaya and Koch (2015) study findings.

Similarly, interviews results can be generalized as lack of accounting education and practical training influences the adoption of IFRS for SMEs in small and medium enterprises sector in Addis Ababa, Ethiopia.

#### **4.3.3.3. Cost of IFRS for SMEs conversion**

The result from table 16 shows that the cost of IFRS for SMEs adoption coefficient is negative and significant at the 5 % significant level. This means that SMEs faces high cost of adopting IFRS for SMEs. This cost factor includes Cost of hiring external consultant or advisor for assisting adoption of IFRS for SMEs is high, Cost of staff training and development is high, Cost of changing or upgrading accounting information system or IT is high, and the other operating

costs. Outstanding among these were, cost of hiring external consultant and cost of staff training and development. This means cost of conversion affects the decision to adopt IFRS for SMEs. Thus, SMEs necessarily bases cost of conversion to decide whether to adopt or not. Therefore, based on the result the researcher rejects the null hypothesis. The finding of this study is consistent with previous studies of Rudzani et al. (2016), Jones and Higgins (2006), De George Ferguson, & Spear (2012), and Uwadiae (2012).

Similarly, interviews results can be generalized as high cost of conversion influences the adoption of IFRS for SMEs in small and medium enterprises sector in Addis Ababa, Ethiopia.

#### **4.3.3.4. Role and enforcement strategies of regulatory body**

Table 16, shows the relationship between IFRS for SMEs adoption decision and the weak Role and enforcement strategies of regulatory body. The Role and enforcement strategy of regulatory body (RENFRS) coefficient is positive and significant at the 5% level. This means the weak Role and enforcement strategies of regulatory body is one influencing factor for the adoption of IFRS for SMEs and SMEs. This can help the researcher to reject the null hypothesis and conclude that there is a significant effect role and enforcement strategy of regulatory body has on the adoption of IFRS for SMEs. Therefore, the greater the role regulatory body plays and better enforcement strategies it implements, the higher the probability of the adoption of IFRS for SMEs by SMEs.

The result of this study is consistent with Arhin et al., (2017), and John Kwaku, Siaw, & Mensah (2019) that regulatory and professional bodies play weak role in regulating & enforcing and do not support SMEs to adopt the standard successfully.

Finally, most interviewees believe that government and regulatory body's efforts are inadequate towards the successful adoption and implementation of IFRS for SMEs.

#### **4.3.3.5. The effect of firms' size, education, awareness, cost of implementation and enforcement strategy**

In addition to the above result in table 15, firm size is used as a moderator variable to examine its effect on IFRS for SMEs adoption decision. Therefore, size of firm was included in the following econometric model. The regression was performed to test the effect of firm size and the above- mentioned variables on IFRS for SMEs adoption.

$$P(\text{IFRS-sme}_i) = \beta_0 + \beta_1 \text{AWARN} + \beta_2 \text{EDUC} + \beta_3 \text{COSCON} + \beta_4 \text{RENFRS} + \beta_5 \text{SIZER} + \varepsilon_i$$

Table 17 Logistic regression result of the model2

Variables	Prediction	Coefficient $\beta$	Significant level (p-value)
AWARN	+	2.848	0.038
EDUC	+	4.136	0.002
COSCON	-	-3.645	0.000
RENFRS	+	2.882	0.034
SIZER	+	4.831	0.000
Dependent variable: adoption level of IFRS for SMEs(IFRS-SMEs)			
Sample size 232			
R2 of Nagelkerke 0.63			

Source: Survey data, 2020

The regression result in table 17 indicated that the model provided a Nagelkerke's  $R^2=0.63$  indicating that the model accounted of 63% of the total variance. The Wald test indicated that the independent variables including size of firm with AWARN p-value=0.018, EDUC p-value= 0.003, COSCON=0.00, RENFRS=0.031 and sizefirm p-value=0.00 had a significant influence on the decision to adopt IFRS for SMEs. Therefore, the researcher concluded that a decision to adopt IFRS for SMEs is influenced by the size of the firm. The finding of this study consistent with previous studies of Leuz (2010), Mukokoma & Tushabomwe (2019), indicating that the adoption of the standard affected by the size of the firm. However, the result of this study is inconsistent with the findings of Eierle & Haller (2009).

Similarly, interviews results can be generalized as size of firm influences the adoption of IFRS for SMEs in small and medium enterprises sector in Addis Ababa, Ethiopia.

## **CHAPTER FIVE**

### **SUMMARY OF MAJOR FINDINGS, CONCLUSION AND RECOMMENDATIONS**

#### **5.1. Introduction**

This chapter begins with summary of major findings. It is followed by implication of the study. Section 5.4 presents the conclusion. Section 5.5 provided the recommendation part and finally section 5.6 presents recommendation for future research.

#### **5.2. Summary of Major Findings**

The hypothesis tested using logistic regression revealed that there are factors affecting the adoption of IFRS for SMEs by SMEs in Addis Ababa, Ethiopia. These factors are; low level of awareness of IFRS for SMEs, low education level and inadequate practical training, cost of conversion, role and enforcement strategy of regulatory body and size of firms. The descriptive statistics showed that the overall mean of respondents in table9, indicates that respondents agreed they are unaware of GAAP, full IFRS and IFRS for SMEs; organization's accounting staff has a limited understanding of IFRS for SMEs adoption process, in their organizations little is known about the benefits of adopting IFRS for SMEs.

With regard to education and training, the overall mean of the result in table 10 indicates that respondents agreed IFRS for SMEs adoption requires a high level of education & well skilled accounting professionals, low level qualification of accounting education is obstacle for the adoption of IFRS for SMEs ,lack of adequate technical capacity for conversion process is a challenge for successful adoption of IFRS for SMEs , low level of education and inadequate practical training inhibits the decision to adopt IFRS for SMEs, and unavailability of training facilities and training center is obstacle to get accountants trained on IFRS for SMEs.

From cost of conversion point of view, the finding result in table 11 indicates that respondents agreed cost of hiring external consultant or advisor for assisting adoption of IFRS for SMEs is high,, cost of staff training and development is high, cost of changing or upgrading accounting information system or IT is high, and the other operating costs, beyond those identified in the

questionnaire associated with adopting IFRS for SMEs could be significant. The researcher therefore concluded that high cost of conversion affects the decision to adopt the standard

The overall mean result of table 12, indicates that respondents agreed little or no effort was being made by regulatory body to encourage adoption of IFRS for SMEs, there is no effective practice review, and monitoring mechanisms that ensure proper and effective adoption and implementation of IFRS for SMEs roadmap, there is lack of technical guidelines, interpretations and other supporting materials in Ethiopian context that assist the successful adoption of IFRS for SMEs, and absence of adequate workshops, seminars, forums to be organized by responsible body affects the successful adoption of IFRS for SMEs. The result of the finding in table 12 also indicates the positive mediation influence of firm size between adoption decision and factors affecting the decision to adopt IFRS for SMEs.

Five hypotheses were developed to test factors that affect the adoption of IFRS for SMEs. The following are the hypotheses that were tested:

H1: Education level & training has no significant effect on the decision to adopt IFRS for SMEs

H2: Awareness of IFRS for SMEs has no effect on the decision of adopting IFRS for SMEs

H3: Size of SMEs has no mediation influence on the relationship between adoption decision and adoption challenge factors

H4: Role and enforcement strategy of regulatory body has no significant effect on the decision to adopt IFRS for SMEs

H5: Cost of conversion has no significant effect on the decision to adopt IFRS for SMEs

The logistic regression result in terms of testing the relationship between IFRS for SMEs adoption decision and factors affecting the adoption decision revealed that awareness of IFRS for SMEs, education and training, role and enforcement strategy, and size of firm showed positive and significant relationship with the dependent variable adoption of IFRS for SMEs. However, cost of conversion showed a significant and negative relationship with adoption of IFRS for SMEs. Therefore, based on the result the researcher rejects the null hypothesis.

Two logistic models were used for the analysis. Each model emphasizes on the research objectives stated in chapter one. The first model used to test the significant relationship between awareness of IFRS for SMEs, education and training, role and enforcement strategy and cost of conversion.

Awareness of IFRS for SME has positive and significant impact on IFRS for SMEs adoption decision. This implies that SMEs lack awareness of the benefit obtained from adopting the standard that may affect businesses from adopting IFRS for SMEs.

Education and training has a positive and significant impact on IFRS adoption. This implies education level and training significantly predicts the adoption of IFRS for SMEs and SMEs base education and training whether to adopt or not to adopt the standard.

Cost of conversion has a negative and significant effect on the decision to adopt the standard. This means cost of conversion affects the decision to adopt IFRS for SMEs. It also indicates that the higher the cost of adoption, the less the likelihood SMES tend to adopt the standard. This implies SMEs base on cost of conversion to decide whether to adopt or not.

The finding indicate that one factor that influenced IFRS for SMEs adoption decision is the weak role and enforcement strategy the regulatory body played. This implies that the greater the role regulatory body plays and better enforcement strategies it implements, the higher the probability of the adoption of IFRS for SMEs by SMEs and the lesser the role regulatory body plays and the weak enforcement strategy it has, the lower the probability of the adoption of IFRS for SMEs by SMEs.

According to the finding of the second model, the other factor that influenced IFRS for SMEs adoption decision is the size of firm. This implies that the larger the firm size, the more it likely to adopt the standard. It also shows that the second model accounted of more percent of the total variance when firm size is included in the model which is an indication of improvement.

### **5.3. Implication of the study**

This part of the thesis summarizes how the study adds to existing knowledge and its major contributions. In terms of how it extends the existing literature, as far as the knowledge of the researcher is concerned, this research is the first study that considers firm size as mediating

influence factor between the decision to adopt IFRS for SMEs and major factors affecting adoption of IFRS for SMEs by SMEs in Addis Ababa. The study was done during the adoption process which is the right time to examine factors affecting the adoption of IFRS for SMEs. Most reviewed literatures used either quantitative or qualitative method of conducting the research; however, this study employed the mixed approach that contains both quantitative and qualitative data.

The result of the study indicates that most SMEs in Addis Ababa, not adopted IFRS for SMEs. According to public interest theory, adopting IFRS standard can serve the public interest by improving the credibility of accounting information to the stakeholders. Moreover, The public interest theory advocate that accounting information has the attribute of a public good; thus need for government regulated supply of accounting information. Therefore, the government and regulatory body (AABE) must develop supporting and enforcement mechanisms for the successful adoption of the standard.

The theoretical contribution of this study is in the form of testing the institutional theory. Even though, the findings of the study showed weak enforcement strategy of regulatory body, it is the pressure that comes from the government and regulatory body that forces SMEs to adopt the standard which is a concept of coercive isomorphism. The study result showed that most SMEs in Addis Ababa face challenges in adopting IFRS for SMES due to low level of accounting education and lack of practical training. According to DiMaggio & Powell (1983), education and training are normative pressures that explain the emergence of many practices like accounting practice. This suggests that the theoretical explanation of adoption of IFRS for SMEs in Ethiopia is normative isomorphism. In the year 2014, Ethiopia changes its accounting system previously guided by no local standard to IFRS. The absence of local standard and the importance of international standard to the economy of the country, Ethiopia mimetic the International Financial Reporting Standard practices. This indicates that the mimetic isomorphism is fully supported.

Accounting standard regulatory body can use some of the findings of the study to frame policies in the adoption of IFRS for SMEs and enforcement strategies. The result of the study reveals that most SMEs require greater monitoring and enforcement from the benefit of the adoption of the standard point of view.

## **5.4. Conclusion**

This study presents the results of an examination of factors affecting the adoption of IFRS for SEMs by small and medium enterprises in Addis Ababa. Most SMEs in Addis Ababa have not adopted the standard. The study concluded that lack of awareness, lack of accounting education and practical training, cost of conversion, weak role and enforcement strategy and size of firm had great effect in adopting IFRS for SMEs by small and medium enterprises in Addis Ababa.

Majority of SMEs in Addis Ababa lacked awareness and until staffs of SMEs have adequate information, understanding and awareness, the adoption of IFRS for SMEs by SMEs in Addis Ababa and in Ethiopia in general is doubtful.

With regard to education and training, majority of SMEs staff lack adequate accounting education and training, this is because of unavailability adequate training materials and shortage of training centers that provide practical training that assists the adoption of the standard. Therefore, the study concluded that lack of accounting education and training is one major factor that influences the adoption process of IFRS for SMEs by SMEs in Addis Ababa.

The result on cost of conversion showed that the high cost of conversion in the SMEs category influences the adoption of the standard. Due to the high cost of conversion, firms hesitate to adopt the standard. Therefore, the study concluded that cost of conversion is one major factor that affects the adoption process by SMEs.

The study also concluded that the result of the findings assist the government and regulatory body in understanding major factors influencing the adoption of IFRS for SMEs.

## **5.5. Recommendations**

What SMEs lack the most is the awareness regarding the International Financial Reporting Standard. According to the results of the study, majority of the SMEs are not aware of what IFRS for SMEs. Efforts towards bringing the awareness of IFRS for SMEs among the firms should be prioritized. This can be done by arranging seminars, training programs and workshops regarding the awareness of IFRS for SMEs and its importance by responsible bodies such as

government and regulatory body. Emphasis should be on the benefits of adoption of IFRS for SMEs.

Accounting professional bodies should assist in developing awareness through workshops and practical training on the adoption process of IFRS for SMEs with affordable price.

More training centers that provide practical training and materials with affordable price should be available in the market. Resources should be made available on different sources such as websites, internet, libraries etc to provide guidance on how to adopt and convert the standard.

SMEs should do their best in developing awareness of their employees towards the standard through organizing the necessary training, accessing materials from internet and made available them in the working environment that assists staffs to have understanding about the standard.

Not to produce information that is not the interest of stakeholders of the firm, to make it easier for SMEs to do business in foreign countries with suppliers and others by producing quality information, and comparability of financial statements produced by the standard will help SMEs to get access to finance from financial institutions, therefore, for SMEs adopting the standard is beneficial.

Based on the significance of size variable in the study, the regulatory body requires a review of a type of firms to adopt IFRS for SMEs in relation to their size.

To ensure the successful adoption of IFRS for SMEs, enforcement activities through onsite inspection and other mechanisms such as collaborating with banks in addition to the collaboration with Ethiopian Ministry of Revenue should be done. This enhances the adoption of IFRS for SMEs by large number of small and medium enterprises.

## **5.6. Recommendations for future research**

This study was conducted on the factors that affect the adoption of IFRS for SMEs by SMEs in Addis Ababa. Future research could be on adoption challenges of IFRS for SMEs by SMEs outside Addis Ababa city. Another area of future research could be the role of professional bodies and IFRS for SMEs adoption decision.

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## APPENDIX

### Appendix 1 Demographic characteristics of respondents

GENDER					
	Description	Frequency	percent	Cumulative percent	
	Male	132	61%	61%	
	Female	83	39%	100%	
LENGTH OF WORK EXPERIENCE					
	Description	Frequency	percent	Cumulative percent	
	Below 5 years	24	11%	11%	
	6-10 years	86	40%	51%	
	11-15 years	70	33%	84%	
	Above 15 years	35	16%	100%	
Education level					
	Description	Frequency	percent	Cumulative percent	
	High school	0	0%	0	
	TVET Diploma	55	26%	26%	
	Bachelor Degree	122	57%	82%	
	Master	38	18%	100%	
Current position in the organization					
	Description	Frequency	percent	Cumulative percent	
	Owner-manger	19	9%	9%	
	Manager	56	26%	35%	
	Accountant	138	64%	99%	
	Budget revenue head	2	1%	100%	

## Appendix 2

Descriptive statistics: To what extent company's awareness of IFRS for SMEs affects SMEs adoption decision in Ethiopia?

Statement		Frequency	Percent (%)	Cumulative %	Mean
Lack of adequate information about the key difference between GAAP, full IFRS and IFRS for SMEs affects the decision to adopt IFRS for SMEs.	SD	17	7.33	7.33	
	D	33	14.22	21.55	
	U	3	1.29	22.84	
	A	100	43.10	65.95	
	SA	79	34.05	100	
	total	232	100		3.82
Limited or no understanding of IFRS for SMEs adoption and conversion process affects the decision to adopt IFRS for SMEs.	SD	14	6.03	6.03	
	D	34	14.66	20.69	
	N	2	.86	21.55	
	A	103	44.40	65.95	
	SA	79	34.05	100	
	total	232	100		3.86
Little or no understanding of the importance of adopting IFRS for SMEs affects the decision to adopt IFRS for SMEs.	SD	13	5.60	5.60	
	D	19	8.19	13.79	
	N	18	7.76	21.55	
	A	80	34.48	56.03	
	SA	102	43.97	100	
	total	232	100		4.03

## Appendix 3

Descriptive statistics: what impact or aid does education level and training have on IFRS for SMEs adoption decision?

Statement		Frequency	Percent (%)	Cumulative (%)	Mean
IFRS for SMEs adoption requires a high level of education & well skilled accounting professionals	SD	25	10.78	10.78	
	D	23	9.91	20.69	
	N	6	2.59	23.28	
	A	116	50.00	73.28	
	SA	62	26.72	100	
	total	232	100		3.71
Absence of qualified accountant in the area of IFRS is obstacle for the adoption of IFRS by SMEs	SD	16	6.90	6.90	
	D	35	15.09	21.98	
	N	19	8.19	30.17	

	A	101	43.53	73.71	
	SA	61	26.29	100	
	total	232	100		
					3.67
Lack of adequate technical capacity for conversion process is a challenge for successful adoption of IFRS for SMEs	SD	11	4.74	4.74	
	D	35	15.09	19.83	
	N	28	12.07	31.90	
	A	96	41.38	73.28	
	SA	62	26.72	100	
	total	232	100		
					3.70
There was no adequate practical training on IFRS for SMEs conversion process prior to its adoption	SD	22	9.48	9.48	
	D	31	13.36	22.84	
	N	18	7.76	30.60	
	A	103	44.40	75.00	
	SA	58	25.00	100	
	total	232	100		
					3.62
Unavailability of adequate training facilities and training center is obstacle to get accountants trained on IFRS for SMEs	SD	27	11.64	11.64	
	D	20	8.62	20.26	
	N	18	7.76	28.02	
	A	115	49.57	77.59	
	SA	52	22.41	100	
	total	232	100		
					3.63

#### Appendix 4

Descriptive statistics: To what extent that IFRS for SMEs conversion cost affects adoption decision by SMEs in Ethiopia?

Statement		Frequency	Percent (%)	Cumulative %	Mean
Cost of hiring external consultant or advisor for assisting adoption of IFRS for SMEs is high.	SD	29	12.50	12.50	
	D	25	10.78	23.28	
	N	16	6.90	30.17	
	A	116	50.00	80.17	
	SA	46	19.83	100	
	total	232	100		
					3.54
Cost of staff training and development is high.	SD	30	12.93	12.93	
	D	25	10.78	23.71	

	N	7	3.02	26.72	
	A	117	50.43	77.16	
	SA	53	22.84	100	
	total	232	100		
					3.59
Cost of changing or upgrading accounting information system or IT is high.	SD	10	4.31	4.31	
	D	41	17.67	21.98	
	N	6	2.59	24.57	
	A	126	54.31	78.88	
	SA	49	21.12	100	
	total	232	100		
					3.70
The other operating costs, beyond those identified in the questionnaire, associated with adopting IFRS for SMEs could be significant.	SD	12	5.17	5.17	
	D	33	14.22	19.40	
	N	37	15.95	35.34	
	A	91	39.22	74.57	
	SA	59	25.43	100	
	total	232	100		
					3.66

## Appendix 5

Descriptive statistics: What is the likelihood that role and enforcement strategy of regulatory body affects the IFRS for SMEs adoption decision?

Statement		Frequency	Percent (%)	Cumulative %	Mean
Little or no effort was being made by regulatory body to encourage adoption of IFRS for SMEs	SD	19	8.19	8.19	
	D	26	11.21	19.40	
	N	13	5.60	25.00	
	A	103	44.40	69.40	
	SA	71	30.60	100	
	total	232	100		
					3.78
There is no effective practice review and supervision mechanisms that ensure proper and effective adoption and implementation of IFRS for SMEs roadmap	SD	22	9.48	9.48	
	D	24	10.34	19.83	
	N	9	3.88	23.71	
	A	105	45.26	68.97	
	SA	72	31.03	100	
	total	233	100		

					3.78
There is lack of technical guidelines, interpretations and other supporting materials in Ethiopian context that assist the successful adoption and implementation of IFRS for SMES.	SD	18	7.76	7.76	
	D	24	10.34	18.10	
	N	10	4.31	22.41	
	A	92	39.66	62.07	
	SA	88	37.93	100	
	total	232	100		
					3.89
Lack of adequate workshops, seminars, forums etc. is barrier for smooth transition & successful adoption of IFRS for SMEs	SD	17	7.33	7.33	
	D	24	10.34	17.67	
	N	13	5.60	23.28	
	A	118	50.86	74.14	
	SA	60	25.86	100	
	total	232	100		
					3.76

## Appendix 8

### Regression analysis results

. pcorr IFRSsmes AWARN EDUC COSCON RENFERS

| IFRSsmes AWARN EDUC COSCON RENFERS

```
-----+-----
IFRSsmes | 1.0000
AWARN | 0.1609 1.0000
EDUC | 0.1746 -0.0752 1.0000
COSCON | -0.4569 -0.0394 -0.1150 1.0000
RENFERS | 0.1581 -0.0192 0.1344 0.0665 1.0000
```

collin AWARN EDUC COSCON RENFERS  
(obs=232)

Collinearity Diagnostics

Variable	SQRT VIF	VIF	R- Tolerance	Squared
AWARN	1.01	1.00	0.9920	0.0080
EDUC	1.04	1.02	0.9605	0.0395
COSCON	1.02	1.01	0.9777	0.0223
RENFERS	1.03	1.01	0.9751	0.0249

-----+-----  
Mean VIF 1.02

Cond

	Eigenval	Index
1	4.2845	1.0000
2	0.2641	4.0278
3	0.2287	4.3279
4	0.1735	4.9689
5	0.0491	9.3398

Condition Number 9.3398  
 Eigenvalues & Cond Index computed from scaled raw sscp (w/ intercept)  
 Det(correlation matrix) 0.9545

logit IFRSsmes AWARN EDUC COSCON RENFERS

Iteration 0: log likelihood = -87.410677  
 Iteration 1: log likelihood = -64.49159  
 Iteration 2: log likelihood = -53.246748  
 Iteration 3: log likelihood = -52.031628  
 Iteration 4: log likelihood = -52.023357  
 Iteration 5: log likelihood = -52.023352  
 Iteration 6: log likelihood = -52.023352

Logistic regression                      Number of obs = 232  
    LR chi2(4) = 70.77  
    Prob > chi2 = 0.0000  
 Log likelihood = -52.023352              Pseudo R2 = 0.4048

IFRSsmes	Coef.	Std. Err.	z	P> z	[95% Conf. Interval]
AWARN	2.729232	1.100503	2.48	0.013	.5722858 4.886179
EDUC	2.576829	1.105236	2.33	0.020	.4106067 4.743052
COSCON	-3.175671	.5375123	-5.91	0.000	-4.229176 -2.122167
RENFERS	2.932087	1.100935	2.66	0.008	.7742949 5.08988
_cons	-7.52618	1.892291	-3.98	0.000	-11.235 -3.817358

logit IFRSsmes AWARN EDUC COSCON RENFERS sizefirm

Iteration 0: log likelihood = -87.410677  
 Iteration 1: log likelihood = -54.188664  
 Iteration 2: log likelihood = -36.344466  
 Iteration 3: log likelihood = -31.639128  
 Iteration 4: log likelihood = -31.504811  
 Iteration 5: log likelihood = -31.50421  
 Iteration 6: log likelihood = -31.50421

Logistic regression                      Number of obs = 232  
    LR chi2(5) = 111.81  
    Prob > chi2 = 0.0000  
 Log likelihood = -31.50421              Pseudo R2 = 0.6396

IFRSsmes	Coef.	Std. Err.	z	P> z	[95% Conf. Interval]
AWARN	2.848495	1.372053	2.08	0.038	.1593208 5.537669
EDUC	4.136095	1.311738	3.15	0.002	1.565136 6.707054
COSCON	-3.64576	.8423765	-4.33	0.000	-5.296787 -1.994732
RENFERS	2.882204	1.356386	2.12	0.034	.2237368 5.54067
sizefirm	4.831217	1.201091	4.02	0.000	2.477121 7.185312
_cons	-12.21026	2.785572	-4.38	0.000	-17.66988 -6.750641

## **Appendix 9 Research questionnaire**

**Addis Ababa University  
College of Business and Economics  
Department of Accounting and Finance  
MSC Accounting and Finance**

### **Research Questionnaire**

Dear respondent:

I am MSC student in Accounting and Finance at Addis Ababa University and currently conducting a study on “Factors affecting adoption of IFRS for SMEs by SMEs in Addis Ababa, Ethiopia”.

This research will try to contribute to the successful adoption of IFRS for SMEs in Ethiopia by identifying the factors that affect its adoption and provide recommendations that could assist in mitigating any existing challenges. I would be grateful if you could support me to carry out my research by completing the attached questionnaire.

The questionnaire should take you about ten to twenty minutes to complete. Answering the questionnaire is voluntary. If you wish to add more comments or ideas, please write on the space provided. The information you provide will be treated as confidential and only summary of the data is included in the study. Please do not include your name or address on the questionnaire.

If the contents of the questionnaire are not clear, please contact me using the following addresses:

Mobile: 0911-18-67-81

Email: [dastamt@gmail.com](mailto:dastamt@gmail.com)

Thank you for cooperation

With best regards

DestaAmenu  
(MSC student)

## QUESTIONNAIRE

### PART ONE/ Demographic information

1. Gender:     Male             Female
2. Working Experience:
 

<input type="checkbox"/> Below 5 years	<input type="checkbox"/> 11-15 years
<input type="checkbox"/> 6-10 years	<input type="checkbox"/> above 15 years
- What is your highest level of formal education?
 

<input type="checkbox"/> High school	<input type="checkbox"/> Bachelor Degree
<input type="checkbox"/> TVET/Diploma	<input type="checkbox"/> Master
<input type="checkbox"/> Other (please specify) _____	
3. Your current position (Job title) in the organization:  
\_\_\_\_\_
4. Number of employees in your company for current year:
 

<input type="checkbox"/> <= 30	<input type="checkbox"/> 30-100
--------------------------------	---------------------------------
5. What is the general adoption progress of IFRS for SMEs in your organization?
 

<input type="checkbox"/> Adopted	<input type="checkbox"/> In progress	<input type="checkbox"/> not ready to adopt yet
----------------------------------	--------------------------------------	---

### PART TWO/ Challenges of adopting and implementing IFRS for SMEs by SMEs

Please **CIRCLE** how strongly you agree or disagree with each of the following statements on a scale of 1 to 5, with 1= **Strongly Disagree**, 2= **Disagree**, 3=**Undecided**, 4=**Agree** and 5= **Strongly Agree**

s/n	Description	S D	D A	U	A	SA
	<b>Please give your opinion on the following statements. Your assessments should be based on the extent to which the following statements describe your organization's awareness of IFRS for SMES adoption and implementation</b>					
1	Organization's accounting staff lacks adequate information about the key difference between GAAP, FULL IFRS and IFRS for SMEs.	1	2	3	4	5
2	Organization's accounting staff has a limited or no understanding of IFRS for SMEs adoption and implementation process.	1	2	3	4	5
3	In your Organization little is known about the benefits of adopting IFRS for SMEs	1	2	3	4	5
	<b>Please give your opinion on the following statements. Your assessments should be based on the impact education level and training has on the Adoption of IFRS for SMEs in your organization</b>	<b>S D</b>	<b>D A</b>	<b>U</b>	<b>A</b>	<b>SA</b>
4	IFRS for SMEs adoption requires a high level of education & well skilled accounting professionals	1	2	3	4	5
5	Low level qualification of accounting education is obstacle for the adoption of IFRS for SMEs	1	2	3	4	5
6	Lack of adequate technical capacity for conversion process is a challenge for successful adoption of IFRS for SMEs	1	2	3	4	5

7	There was no adequate practical training on IFRS for SMEs conversion process prior to its adoption	1	2	3	4	5
8	Unavailability of training facilities and training center is obstacle to get accountants trained on IFRS for SMEs	1	2	3	4	5
	<b>Please give your opinion on the following statements. Your assessments should be based on the idea that high cost of conversion pose a challenge on IFRS for SMES adoption decision in SME</b>					
9	Cost of hiring external consultant or advisor for assisting adoption of IFRS for SMEs is high.	1	2	3	4	5
10	Cost of staff training and development is high.	1	2	3	4	5
11	Cost of changing or upgrading accounting information system or IT is high.	1	2	3	4	5
12	The other operating costs, beyond those identified in the questionnaire, associated with adopting IFRS for SMEs could be significant.	1	2	3	4	5
	<b>Please give your opinion on the role of regulatory body on the Adoption of IFRS for SMEs</b>					
13	Little or no effort was being made by regulatory body to encourage adoption of IFRS for SMEs	1	2	3	4	5
14	There is no effective practice review, and monitoring mechanisms that ensure proper and effective adoption and implementation of IFRS for SMEs roadmap	1	2	3	4	5
15	There is lack of technical guidelines, interpretations and other supporting materials in Ethiopian context that assist the successful adoption of IFRS for SMES.	1	2	3	4	5
16	Absence of adequate workshops, seminars, forums to be organized by responsible body affects the successful adoption of IFRS for SMEs	1	2	3	4	5

**If you have any comment regarding this questionnaire, or any suggestion that contribute to this study, please provide it and it will be taken in to consideration.**

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Thank you for your cooperation!!

## **Appendix 11 Interview Guide questions**

Addis Ababa University  
College of Business and Economics  
Department of Accounting and Finance

### **Interview Questions**

Interview questions on factors affecting the adoption of IFRS for SMEs by small and medium enterprises in Addis Ababa, Ethiopia.

1. How familiar are you with IFRS for SMEs?
2. Do you agree IFRS for SMEs adopted by SMEs properly? If not, please mention the reasons.
3. From your perspectives, what are the main factors that could influence the adoption of IFRS for SMEs by SMEs in Ethiopia?
4. To what extent that the size of SMEs affects the successful adoption of IFRS for SMEs?
5. Do SMEs need additional professional consultation and follow up during the adoption and implementation of IFRS for SMEs? If yeas, do you think cost incurred for consultation is high?
6. To what extent education level and training is necessary for the adoption of the standard? And for whom it is important? Why?
7. To what extent do you need assistant from regulatory body (AABE) at the time of adoption IFRS for SMEs?
8. Does your organization supervised by regulatory body (AABE) for the adoption of IFRS for SMES? If yes How frequent it is?
9. What is the adoption progress of IFRS for SMEs?
10. Do you have any other comments or ideas?

Thank you for your cooperation!