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A Comparative Study on Financial Statements Preparing under CAS and IFRS in Cambodia (A Case of Phnom Penh Water Supply Authority)

Vannida Kimrong

School of Economics and Management
Chongqing University of Posts and Telecommunications
Chongqing-400065, China. Email: k.vannida@icloud.com

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Abstract. This study examines the difference outcome of financial statements were prepared under Cambodian Accounting Standard (CAS) and International Financial Report Standard (IFRS) in Cambodia, as a case of Phnom Penh Water Supply Authority in the purpose of reporting standards is to increase earning management and quality of financial statements. The research undertaken, is based on the comparative index of financial statements of Phnom Penh Water Supply Authority (PPWSA) list on Cambodia Securities Exchanged market. The purpose of comparative financial statements is to investigate the quality of accounting information enhanced in the context of full IFRS adoption in Cambodia at the year-end 2011. Furthermore, financial analysis were conducted by using comparison of financial ratios analysis complying with Cambodia Accounting Standard (CAS) and IFRS. Based on the data analysis in a case of PPWSA, it was revealed that the comparative index of total assets, total liability and total equity come out with the same results after IFRS adoption. The reason is probably because the measurement of recognition of accounting booking, business transactions and the CAS standards itself are equivalent to IFRS standards. However, there are still some items impact on balance sheet statement after IFRS adoption as the results of comparison of financial statements and ratios analysis such as the increase of liquidity and profitability. These results created the good values of financial statements, and might be increased earning managements. The cause of increases are because industries measurement of accounting recognition on assets, liability and the valuation of depreciation on property plant and equipment were prepared differently in both standards. On the other hand, the research observed that there is no impact items on income statement of PPWSA after implementing IFRS.

Keywords: CAS and IFRS adoption, financial statements, earning management, financial report quality

AMS Mathematics Subject Classification (2010): 91G50

1. Introduction

As the coming up of IFRS, the world is at the end of convergence towards this standard which are high quality accounting standards for judging the transparency and comparability of financial statements in financial reporting process. All users of financial statements want a true and fair representation of information about companies in financial statements. However, under the crisis period, it is disputable whether companies present the true position to the users of financial statements to make economic decision and for resource allocation. On the other hand the management of companies can make different accounting choices or structure business transactions to report according to intent rather than true and fair presentation. As the standards are most acknowledgeable, IFRS began as an attempt to harmonize accounting across the European Union and the value of harmonization quickly made the concept attractive around the world such as Brazil, Australia, Canada, India, Taiwan, Japan and so on. And as one of Asian country, Cambodia also becomes IFRS compliant and the standards were renamed as Cambodian International Financial Reporting Standards (CIFRS). The dates for companies to implement CIFRS and CIFRS for SMEs were then set by an announcement/ notification of the Ministry and Economy and Finance dated 28 August 2009. The date for application of full IFRS Standards in Cambodia was set for periods beginning on or after 1 January 2012 and the additional information provided by IFRS organization mention that mandatory implementation of IFRS Standards for commercial banks and microfinance institutions started for periods beginning 1 January 2016 (www.ifrs.org). As Cambodia now belongs to the League of IFRS-adopting countries, perhaps persuaded by the gains it promises, it however remains to be convincingly empirically established the extent to which this set of accounting standards has impacted on financial reporting practices in Cambodia.

Most studies on IFRS have concentrated on it as a financial reporting issue. But financial reporting is one aspect of the total impact of IFRS composition. Much more significant is the impact of a set of standards on a company's organization, philosophy, business structure compliance to the standards, performance management, and internal control and so on. However, financial reports has still recognized as one of the most important part of earning management and it is very important for making business decision, investment, raising fund and it is the tool to bring stakeholders know the health of business. Moreover, the key to economic development is a sound financial reporting system sustained by good governance, clearly defined quality standards and established regulatory framework. Therefore, this study is an attempt to compare the differences of financial report quality under both standards and providing evidence on the impact of IFRS on financial reporting practices in the Cambodia as bring one case of PPWSA.

2. Methodology

The research undertaken, is based on the comparative financial statements of PPWSA listed on Cambodia Stock Exchange market to investigate the quality of accounting information enhanced in the context of Full IFRS adoption at the end of year 2011 and financial analysis has been conducted by using comparison of ratios on financial data under Cambodia Accounting Standard (CAS) and IFRS. Financial ratios are used to analyze the differences between two standards of statement ratios and to figure out the balance sheet and profit and loss statement preparing under IFRS and CAS. The comparative index will be used to compare financial statements such as asset, liability and equity preparing under IFRS and CAS.

a) Comparative financial statement, asset, liability and equity

The financial statements of PPWSA list on Cambodia Securities Exchanged was selected as the case of this paper in view of the criticality of its roles in the Cambodia economy. Comparability of financial report is one of the ways by which IFRS positively impact on financial reports. This study attempts to quantitatively measures the extent to which financial reports were prepared under different accounting standards (CAS and IFRS) can be compared. To this end, a modified version of the Gray's Conservatism Index was used. Gray (1980, as cited in Cardozzo, 2008) first introduced the Index of Conservatism in comparing profits of several countries as a quantitative measure of differences between accounting practices. This Conservatism Index could otherwise be called 'Comparability Index'. This paper modified this Comparability Index by applying it to other key elements of financial statements such as assets, liabilities and equities prepared under CAS and IFRS.

The comparative index will be compared financial statement such as asset, liability and equity preparing under IFRS and CAS. This Index is calculated below:

Total Comparability Index of Asset = 1 – (Total Asset (IFRS) – Total Asset (CAS))/Total Asset (IFRS)

Total Comparability Index of Liability = 1 – (Total Liability (IFRS) – Total Liability (CAS))/Total Liability (IFRS)

Total Comparability Index of Equity = 1 – (Total Equity (IFRS) – Total Equity (CAS))/Total Equity (IFRS)

Furthermore, the benchmark used in this study is IAS/IFRS for evaluating the accounting impacts on the elements of the statements of financial positions of the transition from the CAS to IFRS. The total assets, total liabilities and total equities reported under IFRS are chosen as the denominators in order to assess the impact of IFRS on Cambodia financial statements. The neutral value of the index is one. This implies that there is no impact situation on the CAS by IFRS. An index that is greater than one implies that the Cambodia companies' total assets, total liabilities and total equities are higher than what were reported under IAS/IFRS. Conversely, an index that is lower than one suggests that the Cambodia companies' total assets, total liabilities and total equities are lower than that what were reported under IAS/IFRS.

b) Financial ratios analysis: liquidity and profitability

The study also use financial ratios analysis such as liquidity ratios to analyze these two financial report standards because liquidity ratios are some of the most widely used ratios perhaps similar to profitable ratios. They are especially important to creditors. These ratios measure a firm ability to meet its short-term obligations. By applying these ratios in this research, it is required to have the balance sheet statement.

Moreover, the ratios that managements use the most is profitability ratios and they are applied in this research as well. The profitability ratios are mostly use in investment analysis because these ratios measure the firm's ability to earn an adequate return. The profitability ratios need some relevant data such as financial position, income statement or statement of earning equity.

Here are financial ratios that were conducted in this study:

Liquidity ratios

- Current Ratio (time) = Current Asset/Current Liability
- Acid Test Ratio (time) = (Cash + Accounts Receivable + Short-term Investments) / Current Liability

Profitability ratios

Margin Ratio

- Gross Profit Margin (%) = Gross Profit/Net Sales
- Net Profit Margin (%) = Net Income/Net Sales

Return Ratio

- Return on Assets (%) = Net Income/ Total Assets
- Return on Capital Employed (%) = 100 x Operating Profit/Capital Employed
- Return on Shareholder Equity (%) =Net Income (Annual)/Average Shareholders' Equity

3. Data and analysis

It is essential to note that these data were gleaned from the annual reports of PPWSA for the year end 2011. The annual reports for year 2011 were prepared by PPWSA in compliance with the Cambodia Accounting Standard and therefore, the Cambodia total assets, total liabilities and total equities as at December 31, 2011 were obtained from here. As the announcement from World Bank financial reports, all big companies have to prepare their financial reports compliant with IFRS standards starting from or after Jan 01, 2012 so the data of company's financial report at the end of year 2011 that prepared under CAS are equivalent to financial report prepared under IFRS on Jan 01, 2012.

Table 1: The comparative index of PPWSA's total assets at the Year End Dec 31, 2011

Total Assets				
Company	**IFRS**	**CAS**	**Difference**	**Comparability Index**
	KHR	KHR	KHR	
PPWSA	865,250,609.00	865,250,609.00	0	**1**

Table 2: The comparative index of PPWSA's total liability at the Year End Dec 31, 2011

Total Liabilities				
Company	**IFRS**	**CAS**	**Difference**	**Comparability Index**
	KHR	KHR	KHR	
PPWSA	312,822,128.00	312,822,128.00	0	**1**

Table 3: The comparative index of PPWSA's total equities at the Year End Dec 31, 2011

Total Equities				
Company	**IFRS**	**CAS**	**Difference**	**Comparability Index**
	KHR	KHR	KHR	
PPWSA	552,428,481.00	552,428,481.00	0	**1**

Interpretation

From table 1, 2 and 3, the comparable index of data analysis of total assets, liability and equity of PPWSA, the results are equal 1 all among three items so it indicated that there is no any impact on Cambodia financial reports after adopting international financial report standards. It maybe because in that year of new reform to IFRS, some transactions of company recorded, were not applicable to the IFRS Standards. There are a lot of standards of IFRS approximately 54 standards that those have clearly interpreted which business transaction to be recorded as. As in equity statement, there were not presented details of items relevant to stock or stakeholder share that's why there was hard to find the difference in both standards. Cambodia securities market is quite new to all companies who selling stocks as it was found in Jul 11, 2011, five months before mandated the IFRSs adoption in Cambodia and PPWSA is the only first company who was called for stock exchange institution. Moreover, based on the comparative index of total asset, total liability and total equity of PPWSA, it can interpret that the financial position that prepared under CAS are qualify to those some standards of IFRS. Even though the comparable index showed that there are no effect of financial statements after IFRS adoption, there are still some variant items in financial position statement were changed after reported to IFRS such as measurement of recognition in current assets, non-current asset and current liability and non-current liability, so these variation of items will be discussed in financial ratio analysis.

Interpretation of asset items

Table 4: An asset is a resource or a wealth controlled by the entity arising from past events and from which economic benefits are expected to flow to the entity in the future. As per IFRS and CAS of Phnom Penh Water Supplies Authority, the financial statement shows that the total of asset between these two reports are equally but the differences are the current asset of inventory that prepare under Cambodia Accounting Standard is greater than prepare under international financial report standard 28,088,571>27,078,394 KHR that make total current assets of CAS greater than IFRS. In contrast, none current asset of property, plant and equipment which prepare under CAS is less than prepare under IFRS 633,395,921<632,385,744 KHR, the differences are from the recognition of each account treatments by reverse the amount of current asset to non-current asset after adoption IFRS standard. And additionally, the recognition of property, plant, equipment and inventories in both standards are contrary or it's probably the account technique of managements by using these account recognition assumption as their advantages to present their financial statement relating to asset and liability.

Table 4: Comparative consolidated balance sheet of PPWSA under CAS and IFRS

PHNOM PENH WATER SUPPLY AUTHORITY Statement of Financial Position as at the End of Dec 31, 2011			
	CAS KHR	**IFRS KHR**	**Increase/ Decrease %**
Property, plant and equipment	632,385,744	633,395,921	0.16
Intangible assets	1,033,905	1,033,905	0
Loan to Pursat Water Supply	703,161	703,161	0
	634,122,810	635,132,987	0.16
Current assets			
Inventories	28,088,571	27,078,394	-3.6
Trade and other receivables	40,095,235	40,095,235	0
Loan to Pursat Water Supply	62,452	62,452	0
Short-term investments	151,799,927	151,799,927	0
Deferred IPO cost	3,620,793	3,620,793	0
Cash and cash equivalents	7,460,821	7,460,821	0
	231,127,799	230,117,622	-0.44
Total assets	865,250,609	865,250,609	0
EQUITY AND LIABILITIES			
EQUITY			
Capital	465,028,129	465,028,129	0
Reserves	55,410,445	55,410,445	0
Retained earnings	31,989,907	31,989,907	0
Total equity	552,428,481	552,428,481	0
LIABILITIES			
Non-current liabilities			
Retirement benefit obligation	24,601,028	24,601,028	0
Deferred income tax liabilities	16,935,710	16,935,710	0
Borrowings	182,847,463	182,847,463	0
Refundable water deposits	24,602,071	24,602,071	0
Deferred government and other grants	7,535,667	7,535,667	0
Performance guarantee		7,192,923	100%
	256,521,939	263714862	2.8
Current liabilities			
Borrowings	11,504,413	15,019,945	30.56
Income tax payable	437,665	437,665	0
Accrual for IPO fee	3,215,717	3,215,717	0
Trade and other payables	41,142,394	30,433,939	-26.03
	56,300,189	49,107,266	-12.78
Total liabilities	312,822,128	312,822,128	0
Total equity and liabilities	865,250,609	865,250,609	0

Interpretation of liability items

Liability is an obligation. A liability is a present obligation of the entity arising from past events, the settlement of the obligation results in an outflow from the resources embodying economic benefits. Obligations of a business include the amounts owing to lenders or any other entity for loan taken and the amount owing the suppliers for goods purchased on credit. According to the statement of balance sheet of PPWS authority, total liability reported under both standards, IFRS and CAS, it shows that the total of liability between these two reports are completely differences. The study observed that there is no recording the amount 7,192,923 of performance guarantee in non-current liability prepared under CAS but on the another hand, it was been recorded in liability of IFRS statements. In the meantime, the recording of borrowing amount of current liability that are prepared under CAS is less than IFRS 11,504,413<15,019,945 and the amount of trade and other payables prepared under CAS is more than IFRS 41,142,394>30,433,939. The research found that the number of differences in current liability as the same as non-liability after IFRS adoption. It means that after mandated IFRS, the non-current liability has increased to 7,192,923 KHR, meanwhile the current liability has decreased 7,192,923. So these variance of account recognition of current liability and non-current liability and all accounting treatments under both standards will make the problems or the risk to tax authority or company its self.

Interpretation of equity items

Equity is the residual interest in the assets of a business organization after deducting all its liabilities. Assets minus liabilities equal equity. At the same time, it does not mean that asset cannot be divided into sub classifications that are shown separately in the balance sheet. The amount, at which equity is shown in the balance sheet, depends on the measurement of assets and liabilities. The aggregate amount of equity coincidentally corresponds with the aggregate market value of the shares of a business entity or the sum that could be raised by disposing the net assets. As the comparison of statement of equity prepared under IFRS and CAS in PPWS authority, the total equity prepare under CAS are the same to the total equity were prepared under IFRS 552,428,481= IFRS 552,428,481 KHR. So there were no significance differences between the CAS and IFRS treatment of equity statement. .

As the research study on income statement, there are no impact observation of income statement preparing under IFRS and CAS as company its self (PPWSA) was mentioned that there are no coming standards of IFRSs were applicable for their profit and lost report transaction. The below is the statements from Phnom Penh Water Supply Authority were stated in company’s financial statements at the year ended 31 December 2012 on page 27.

Transition to CIFRS

The PPWSA’s financial statements for the year ended 31 December 2012 are the first annual financial statements prepared in accordance with CIFRS.

The PPWSA’s CIFRS accounting policies presented in Note 2 have been applied in preparing the financial statements for the year ended 31 December 2011, the corporative information and the opening statement of financial position.

Table 5: Comparative consolidated P&L account of PPWSA under CAS and IFRS

PHNOM PENH WATER SUPPLY AUTHORITY Income Statement for the Year Ended December 31, 2011			
	CAS	**IFRS**	**Differences**
	KHR	**KHR**	**%**
REVENUES			
Sales	114,868,279	114,868,279	0
Other income	212,052	212,052	0
	115,080,331	115,080,331	0
EXPENSES			
Depreciation and amortization charges	(21,239,491)	(21,239,491)	0
Electricity cost	(22,809,698)	(22,809,698)	0
Salaries, wages and related expenses	(18,971,337)	(18,971,337)	0
Raw materials for water treatment	(4,462,250)	(4,462,250)	0
Raw materials household water connections	(5,126,863)	(5,126,863)	0
Repairs and maintenance	(2,907,029)	(2,907,029)	0
Other operating expenses	(2,709,243)	(2,709,243)	0
Foreign exchange gain – net	2,340,812	2,340,812	0
	(75,885,099)	(75,885,099)	0
Operating profit	39,195,232	39,195,232	0
Finance income	6,462,020	6,462,020	0
Finance cost	(5,600,458)	(5,600,458)	0
Finance income – net	861,562	861,562	0
PROFIT BEFORE INCOME TAX	40,056,794	40,056,794	0
Income tax expense	(8,066,887)	(8,066,887)	0
NET PROFIT FOR THE YEAR	31,989,907	31,989,907	0

The effect of the PPWSA's transition to CIFRS is summarized as follows:

i) Transition elections

Upon transition, CIFRS 1 permits certain exemptions from full retrospective application. The PPWSA has elected not to take any of the optional exemptions available under CIFRS 1, except for "Day One" profits as discussed below. In addition, none of the mandatory exemptions are applicable to the PPWSA.

There is an exemption for the recognition of "Day One" profits to be applied prospectively for transactions, such as loans obtained at an interest below market rate, entered into after the date of transition to CIFRS.

ii) Reconciliation of equity and comprehensive income previously reported under CAS to CIFRS

The PPWSA implemented early adoption of some accounting standards (CIAS 19 – Employee benefits, CIAS 23 – Borrowing costs and CIAS 34 – interim financial reporting) in previous years, although the financial statements for those years were prepared under CAS. As a result, there are no significant differences in the equity reconciliation for the transition.

Table 6: Comparison of ratios as per value of PPWSA under CAS and IFRS

Ratios	As CAS	As IFRS	% Differences
Liquidity Ratios			
Current Ratio	4.11	4.69	14.15
Acid Test Ratio	3.54	4.06	14.66
Profitability Ratios			
Return on Capital Employed	4.85	4.80	-0.88
Return on Shareholders’ Equity	0.04	0.04	0.00
Return on Assets	0.04	0.04	0.00
Gross Profit Margin	1	1	0.00
Net Profit Margin	0.28	0.28	0.00

Table 6 showed the comparison results of ratios as per value of PPWSA under CAS and IFRS. There are two types of financial ratios that were selected to analyze in this study, the liquidity ratios and profitability ratio. There are two components of liquidity ratios such as current ratio and quick ratio/acid test ratio that were used to analyze due to the available of data. There are four items of profitable ratios that were chosen to analyze such as return on capital employed, return on shareholders’ equity, return on assets, gross profit margin and net profit margin.

Interpretation of liquidity

First of all let see the analysis of liquidity analysis. The research observed that the amount of current assets in the two sets, CAS and IFRS are quite differences. The differences because the amounts of current assets and currents liability that reported under both standard varies such as the recognition of inventories, short term borrowing and trade and other payables were changed after IFRS adoption. This’s probably due to the variations in recognition of certain items of these two standards measure differently according to owned standards have been set. For liquidity ratios, the current ratio of CAS is 4.11 but 4.69 after IFRS adoption. The percentage differences of the current ratio is 14.15% were improved in the case of IFRS adoption which shows that IFRS are more value compared to CAS.

In the meantime, relating to cash, account receivable and short term investment compare to current liability, the acid test ratio of CAS is 3.54 and 4.06, after IFRS implementation, the percentage of increased while using IFRS reached to %14.66. The reasons are because the measurement recognition of the current liability under IFRS are less than CAS while the elements of asset such as cash, account receivable or short-term investment that compliant with both IFRS and CAS remain the same. These results would be the best choice of management to pay high attention to IFRS as the accounting technique that can present liability low and this coming out is probably increase earning managements.

Interpretation of profitability

The last financial ratio that would be taken to interpret is profitability. The return on capital employed, return on shareholders' equity are good indicators of profitability. For return capital employed as CAS preparation is 4.85 while after IFRS preparation is just 4.80. In this component, when applied IFRS standards, the earning management was decreased but if comparing the percentage of decreased, it is not that much just only %-0.88. These changed because of the variation of current liability adopted complying to CAS and IFRS effected to the return on capital employ while other accounts are still presenting the same such as total assets and operating profit. For return on shareholder's equity, there are no differences that can be observed. As return on shareholder's equity of CAS and IFRS are equal to 0.04. It might be because the ways of recognition of return on shareholders' equity prepared under CAS equivalent to IFRSs standards.

At the same time of return on assets, gross profit margin and net profit margin, these three components of profitability ratios were found that there is no any impact observation on financial report quality after IFRS adoption. It is because the profit and loss statement of PPWSA that were reported as CAS and IFRS are equivalents in the recognition of all components in income statements such as sale revenues, cost of sale, net income and total assets in balance sheet statements. So all these results can be interpreted that IFRS standards have no any effect on return on assets gross profit margin and net profit margin that were prepared under CAS standards.

4. Conclusion

As Cambodia is a developing country and striving ahead on the way of economy progress, Cambodia is trying to unify its self with global investments and working hard on how they can work together with foreign investments and as well as the gross border countries. By these objectives, all Cambodia corporations; public sectors and private sectors need the global accounting standards for their financial reporting. Again, in Jan 01, 2012, full IFRS standards were mandated to adopt for all large entities and IFRS for SME and this period of adoption is about 6 months later after the Cambodia Securities Exchanged was founded. The aims of bringing IFRS standards are probably because the transparency, comparable and understandable of financial statements for selling/buying stocks or issuing bonds and might be for fairly presenting of accounting transactions and information for tax paying and reviewing. The research study of comparing financial statements reported under CAS and IFRS will create a win-win situation for all sectors of the economy, the public accounting and the corporate accounting. For the private sectors, as the case study of PPWSA that was discussed on the paper, the comparative index of financial statements such as total assets, total liability and total equity showed that there are no effects on financial report after IFRS adoption. On the other hand, the study of financial ratio analysis found out that IFRS implementation had some good effects on various items of the financial statements and its effects on some powerful ratios. This research helped managements get to know the effects of IFRS standards on financial reports that was forced to mandate in Cambodia such as the increases of liquidity and profitability, the unchanged of items in equities and the effects of conversely recognition of asset and liability items under both standards. And as IFRS is one of the well-known financial report standards around the world, it may bring Cambodia to get boost of investments from across border countries, the trustworthy on Cambodia security market, the transparency and capability of financial statements for internal or external audit purpose compare to CAS. The presents for all fair information and the reliable of financial performances as well as accounting transactions of entities to public sectors will assist for the economic growth, improving the public services, and time consumption of auditing frauds or errors. Even though full IFRS only required large companies must be mandated, the small and medium entities should consider and review back to comply with full IFRS standards as the companies will get the benefits from it.

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