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HIGH QUALITY FINANCIAL REPORTING IN THE FUNCTION OF COMPANY GROWTH IN SERBIA

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Abstract:

The accounting profession and financial reporting quality development are moving alongside market economy development, which contributes to financial system stability and increases capital market efficiency and the efficiency of the entire economy. This paper researches the influence of certain factors on financial reporting quality improvement in Serbia. The paper aims to identify the restrictions and problems in IAS/IFRS application, determine the effect of the factors with the most significant influence and recommend solutions for competent government institutions to establish quality financial reporting systems that will significantly contribute to local enterprise international competitiveness growth and increase. Results of the conducted empirical research showed numerous weaknesses in the system of financial reporting in the Republic of Serbia, which are reflected in frequent changes in legal regulations, small participation of the accounting profession in the enactment of legal regulations, often selective application of IFRS, the absence of national accounting standards, insufficient practical education and improvement of accounting personnel, unadjusted Legal Regulation with EU Directive 2013/34EU and others. Therefore, at the end of the paper, recommendations were given to the competent institutions in the Republic of Serbia to improve and modernize the field of financial reporting, which would affect companies' performance on domestic and international markets.

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INTRODUCTION

Financial reporting represents a direct product of the accounting reporting system which, in its essence and purpose, portrays the performances and achievements of a company in a certain period, its financial and structural position, and its liquidity position on the selected data for the basic accounting rules. The primary purpose of their compilation is reflected in the information service of various interest groups, which rely on them in the business decision-making process. Financial reporting supplies vital information to all existing and potential participants in the financial market, declaring itself a significant factor stimulating its functioning.

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Financial reporting is gaining importance, especially with the appearance of corporate companies and capital market development. Management professionalization caused by ownership separation from the company management and ownership dispersion significantly removing the shareholders from real situations has extended the importance of financial reports/statements. The need to render the accounts on company and management achievements and provide impartial, reliable and relevant information for important business decision-making (on investment, disinvestment, borrowing, loan approving, etc.) caused the financial reports to be the primary source of information for the shareholders, creditors, employees, business partners, management and other interest groups.

National accounting legislation harmonization with international standards is also crucial for developing countries because they need foreign capital for speedy economic development. Serbia has introduced mandatory application of IAS/IFRS for all since 2004, for banks and other financial institutions since 2003. The harmonization process leads to financial reporting quality improvement and direct and indirect benefits for the country that has opted for the procedure. This process is equally important for the SME sector and large companies. The biggest problem in the financial reporting harmonization process in Serbia so far is that legislation often has priority over professional regulation, leading to the slowdown of the process and incomplete IFRS application.

We reviewed the level and quality of financial reporting in Serbia and the implementation of IFRS, which has been there for around 20 years.

A particular aspect is placed on the factors that most affect the successful implementation of IFRS, from the accounting profession, management, legal regulations, and the success of the harmonization process with international standards. Given that the respondents were accounting managers, finance managers, and directors with more than three years of experience in accounting, we believe that through this research, we have reached relevant answers based on which we give appropriate recommendations to the competent state authorities and professional associations that enact legal regulations in the field of accounting and financial reporting.

The first part of this paper indicates the importance and role of high-quality financial reporting in modern situations. The second part of the paper presents the current financial reporting status in the Republic of Serbia. The third part contains research results on the influence of various factors on the financial reporting quality in Serbia, along with recommendations for improving the process and financial reporting quality improvement.

LITERATURE REVIEW

Financial reports enable us to perceive a company's property, liabilities, capital, cash flow, cost, income, profitability, and financial structure movement. The connection between the appropriate information in them can help consider the company's yield, property, and resource management efficiency and its exposure to long-term and short-term financial risks. Reporting on the company's performance facilitates the identification of the most productive capital usage areas, thus making resource allocation more efficient. Financial reports present the results achieved in the previous period, but they also represent the starting point for correct estimates development on the company's perspective and future performances.

Financial reporting primarily aims to create valuable information for financial decision-making. In doing so, the investors, creditors, and other external stakeholders' decisions should be considered.

They have different information needs depending on the nature of the decisions made on the obtained information. It is in the investors' interest to create a portfolio consisting of such investments which direct capital to the areas of its most profitable usage.

The goal of financial reporting (general purpose) is to provide financial information about the reporting entity that is useful to current and potential investors and creditors in the decision-making process related to providing resources to the reporting entity (IFRS - Conceptual Framework for Financial Reporting, 2018).

The aim of IFRS adoption and application is the provision of high-quality financial reports for the business entity and their comparison to its financial reports from the previous billing periods, as well as the financial reports of another (comparable) business entity, regardless of its head office and location. Financial reporting connects top management and executive activities, providing vital information for internal and external users. Therefore, a strong connection is necessary between financial reporting – financial market efficiency – market economy development (Gajić & Medved, 2014).

All informational inputs that can be collected from those primarily responsible for the quality and creative accounting practice are essential. (Dichev *et al.* 2016). Stiglitz (2017) believes that the role of regulation, public policies and institutions in setting the "rules of the game" is very important in information management. The risks of manipulations in financial reports are by no means negligible (Malinic, 2015). According to Gebhardt, Mora & Wagenhofer (2014), the possibility of subsequent verification of accounting information is less important for capital allocation than for effective contracting and evaluation of management's performance. On the other hand, Lindahl & Schadéwitz (2013) expressed doubts about the assumption that legal systems can explain differences in the quality of financial reporting systems.

The primary advantages of financial reporting standardization are (Alihodžić, 2018): financial report transparency, simplified business monitoring for the companies with branches in other countries, the incentive to market integration, and reliable information assurance with the aim of investment decision-making. Several factors influence the delayed implementation and financial reporting harmonization process, such as domestic legislation, achieved level of economic development, regulated or unregulated financial report form, report-keeping deadlines, capital market rules, tax regulations, etc. The complexity of standard implementation in domestic legislation, the influence of domicile tax regulation, frequent standard changes and issues with their interpretation, demands for standard application regardless of the company size, etc. are all indications of the drawbacks of financial reporting standardization.

Low-quality financial reporting causes a lousy practice of corporate management because the foundation of any corporate management structure is the publication of reliable and authentic financial information. Transparency is the foundation for public trust in the corporate system, and the funds will flow into the centers of economic activities, encouraging trust. Although it has never had its own objectives, financial reporting has always been necessary for the market economy to operate effectively. (Djukić & Pavlović, 2014).

The problem of competence in preparing and compiling financial reports goes beyond corporate management and owners (Malinić, 2014). Investors promptly "punish" companies if they fail to meet their expectations regarding the number of accounting profits (Skinner & Sloan, 2002). Biddle, Hilary & Verdi (2009) showed that financial reports of better quality contribute to more efficient investment by limiting overinvestment and encouraging investment in companies in which it isn't sufficient.Investors who do not have access to privileged information cannot be completely protected from opportunistic insider manipulations (White, 2020).

Quality accounting information can be defined as a faithful presentation of the characteristics of the fundamental earning process of the company, which are relevant for making a concrete decision (Dechow, Ge & Schrand, 2010a). The benefits of greater credibility of financial reports exceed informational losses caused by delayed recognition of good news, so this way, conservatism can be considered a system that creates value (Barker & McGeachin, 2015). While on the one hand, there are attitudes that fair value better reflects the risks inherent in reporting entities and their economic performance, opponents of this concept believe that using the fair value reduces the reliability of accounting information and increases the risks of manipulations (Defond *et al.*, 2020).

The more developed an economy is, the more important it is to high-quality financial reporting. Market economy development goes hand in hand with accounting profession development and financial reporting quality. The investors opt for the markets they are familiar with and have more confidence in the countries that adopt and apply international financial reporting standards. Providing information based on high-quality, transparent and comparable standards considerably reduces the investment risk and capital acquisition cost.

Financial reporting based on clear rules makes it easier for the management to fulfil set responsibilities and for all other users in business decision-making. Unique rules create the possibility of securing order in the field of accounting in the broadest sense and better control of all who want to deviate from the rules defined in that way. Accounting as a function and profession should provide efficient communication between the capital owner and management responsible for high-quality management and disposal of the invested capital.

Managers will be more motivated to make voluntary disclosures to reduce information asymmetry if they have access to privileged information. At the same time, conservatism will persist as a control mechanism to prevent opportunistic behavior (Mora & Walker, 2015). A large number of studies have shown that the obligations of companies, which arise from credit agreements, have an impact on the choice of accounting policies in terms of a more conservative approach to financial reporting, which is a consequence of the realization of creditors' information rights (Tan, 2013; Jayaraman & Shivakumar, 2013; Haw, Lee & Lee, 2014).

Lim & Chang (2017) found that targeted companies opportunistically manage published earnings to achieve a higher acquisition price and that excessive manipulation reduces the quality of financial statements. Enomoto, Kimura & Yamaguchi (2015) concluded that the management of accounting components of profit is expressed in economies with weaker protection of investors' rights and a lower degree of "the rule of law" and vice versa.

Conclusion about the positive connection between the quality of accounting gains and profitability performance prevails in the scientific accounting literature. In addition, Ma & Ma (2017) evaluated the persistence, predictability, and discretionary components of accounting results on a sample of 7,921 company years of observations from the Chinese securities market, providing empirical support for the finding that more prosperous businesses have lower-quality reported earnings.

Managers try to hide extremely high profits by making reserves for periods in which, by breaking them down, they will be able to balance out undesirable declines in results. According to Lee & Richie (2016), there are two schools of thought on what motivates managers to implement this strategy. The first school believes that balancing gains is an effective means of communicating privileged information, bearing in mind that the investment public can more easily make projections of future performance based on balanced gains. Another school of thought considers motivation to be advancing managerial careers and increasing compensation by changing the perception of financial performance.

The differences among the accounting practices in the countries are the main reason for the inability to compare the companies' capital value and business results in various countries. These differences reduce the national market and capital efficiency slowing down the internalization of capital flows. In this situation, the investors become the key instigators of changes in financial reporting to create a single financial reporting system and disclosing information worldwide. Accounting systems differ between and within countries, and individual companies may use different accounting systems for other purposes (Nobes & Parker, 2016, p. 28).

The international standards in financial reporting are standardization instruments at the global level and facilitate international communication. The country providing high-quality accounting reporting according to IAS/IFRS gains the following advantages: increases its capability to take part in the global capital market, encourages capital inflow to the country, simplifies demands about reporting, simplifies the possibility of international comparison, reduces the cost of adjustments to quality financial reporting demands and their necessary continuous improvement, encourages the access to capital markets around the world and directly increases the efficiency of its own securities market, etc.

Financial accounting and reporting practices are dynamic responses to the changeable micro and macro conditions, including political, economic, fiscal, and trade changes. Likewise, the companies represent a part of society, and history, institutions, and cult expectations of society influence their corporate business. The survival of any business entity depends, more or less, on the international market.

In recent years, investots have asked for information on development strategy, domestic and foreign environment, business entity goals, asset structure, value, etc. Their demands also expand to additional business information so that accounting reporting grows into business reporting. Investors expect timely, clear, consistent, and objective information in financial reports. This is the only type of information to make a healthy foundation for business decisions in the current competitive situation. Harmonization between accounting and audit practices is essential because it facilitates accounting and financial communication between business entities worldwide, thus bridging financial barriers to achieving a higher degree of freedom in goods, services, and capital flows (Leković & Arsenović, 2013).

The provision of fair and high-quality financial reporting implies respect not only for legal but also for ethical standards. Professional and legal regulations represent minimum standards of behavior for professional accountants and all those who participate in financial report making, and ethics are added to it (Malinić, 2011). Blurring and faking results lead to investors' decisions that are not in the function of efficient capital allocation. Accurate and fair financial reporting is a first-rate public interest (Stevanović, 2011), therefore the principle of objective reporting should be the guiding principle for financial report creators.

External experts (auditors) are hired to audit financial statements and data disclosed by the management and to offer an expert opinion on whether the financial reports in all material respects present realistic and objective business results of a company in a certain period (income statement) and its financial position on a specific day (balance sheet) in order to increase the level of confidence that users have in the financial reports.

Management decisions are based mainly on the information coming from the accounting system. Managers should work for the shareholders and subordinate their interests to the company's interests. Still, in practice, managers often work in their own interest, which can make their decisions suboptimal from the aspect of shareholder and employees' well-being. This problem is well-known as the agency problem. Therefore, the shareholders should control management activities regularly, which is conducted most successfully through independent external audit engagement (Žarkić *et al*, 2013).

Rapid globalization processes and international activities in the recent years have imposed an increasing need for accounting and financial reporting harmonization in the SME domain. Undeniably, their influence increases yearly, and they represent a development generator, especially in countries in transition. The same legislation is applied to SMEs and large companies in certain countries, but many countries have unique national standards for micro, small, and medium enterprises (Žager & Dečman, 2015). Due to the increasing share of SMEs in the international market, there is a need for financial reporting harmonization in this sector. The result of the harmonization should be business performance improvement in these companies and easier integration in the developed international market.

The complete application of IFRS causes practical problems in many companies due to their complexity, lack of appropriate personnel and financial assumptions, so the IASB started the work on simplified standards at the beginning of the 20th century required for these companies.

The International Accounting Standards Board adopted the international financial reporting standards for small and medium-sized legal entities (IAFS for SMEs) in 2009 to address the requirements of small and medium-sized businesses publishing general purpose financial reports (FR) for external users without public responsibility. Through the modification and simplification of thorough International Accounting Financial Standards (IAFS), these standards were developed.

In the process of specific accounting policy selection, the management applies, among other things, the principle of clarity and caution in rating: the income should not be overestimated, nor expenses or liabilities underestimated. Also, the principle of a substance above form: business events should be shown according to their financial substance, not exclusively according to their legal form. Having the appropriate accounting policy is essential for small and medium-sized enterprises because they frequently struggle to completely comply with demanding international standards due to a lack of accounting staff. So, audit aid on these issues is vital for these companies.

One of the requirements relevant to raising the level of quality and transparency of financial statements refers to the auditor's opinion, so companies that wish to be included in the Prime Listing are required to have a favourable opinion from an authorized auditor for financial statements prepared for the business year preceding the submission of the request. At the same time, a modified opinion is also allowed to include the company in the Standard Listing (Belgrade Stock Exchange, 2018, art. 6).

Barac *et al.* (2017) found that accounting manipulations in Croatia were aimed at three groups of users: suppliers, tax authorities, and creditors. Carson *et al.* (2016) found that the % of modified opinions on financial statements increased during the major financial crisis after 2008. According to the European Commission Report (2017), the big four audit firms have an average market share of almost 70% in the EU mandatory audits of listed companies. In Slovenia, all listed companies were audited by the big four (Stager & Odar, 2017), while on the Serbian regulated market, only around one third of enterprises were audit clients in 2014 and 2015 (Vučković Milutinović, 2019).

Characteristics of the macro-economic environment, corporate culture, and the regulation of the financial reporting system led to the fact that, in the World Bank Report concerning the observance of accounting and auditing standards and codes, the quality and reliability of financial reporting in the Republic of Serbia were assessed as unsatisfactory (World Bank Group, 2015, p. 43).

THE CHARACTERISTICS OF FINANCIAL REPORTING IN SERBIA

National accounting regulation harmonization with international standards is essential transition countries requiring foreign capital for accelerated economic development. According to Mitrović (2013), international accounting regulation is a quality factor in financial reporting on the one hand and the instrument of financial reporting harmonization on the other hand. However, these facts are often ignored in practice, so the harmonization process with the international regulation is considered an additional liability to be adjusted to, the fulfillment of regulations, etc.

IFRS has been mandatory in Serbia since the beginning of 2004 for banks and other financial organizations since 2003. It is introduce to harmonize the accounting system with the generally accepted international achievements in this field. The application of these standards provides comparability of financial reporting business entities with other business entities in the country and abroad, and that is very important from the financial market functioning perspective because the participants in this market need relevant and reliable information on the financial position and the entire business of securities listed in the market.

The Law on accounting (the Official Gazette no. 73/2019 and 44/2021) says that small and medium-sized business entities apply the IFRS for financial reporting positions recognition, evaluation, presentation, and disclosure and that the standard could be applied by micro and other business entities. If we start from this point, there are three bases for FR position recognition and evaluation in the Republic of Serbia, and they are:

1. Full IFRS, including the International Financial Reporting Standards (IFRS) and the International Accounting Standards (IAS) with the framework for financial reporting preparation and presentation as well as its interpretations, issued by those regulating the standards ('RS Official Gazette' no. 35/14);
2. Specific IFRS for small and medium-sized business entities ('RS Official Gazette' no. 117/13); and
3. The manual on position acknowledgement, evaluation, presentation, and disclosure in the individual financial reports about micro and other business entities ('RS Official Gazette' no. 118/13, 95/2014), issued by the Ministry of Finance of the Republic of Serbia.

All business entities, independently from the one already applied, must create a general act on the accounting policies according to the accounting basis they apply (full IFRS, IFRS for SM business entities, or the manual for micro and other business entities), where they edit the issues of accounting estimation changes, the ways to correct the mistakes from earlier times as well as the applied accounting policies.

According to Article 6 of the Law on accounting, business entities are classified according to size: 1) micro, 2) small, 3) medium-sized, and 4) large, based on the data from the regular annual financial report for the previous year. The criteria for selection according to size are the average number of employees, business income, and average business property worth, established on the day when a regular annual financial report is compiled.

Table 1. Business entity classification according to Article 6 of the Law on accounting

Business entity size	Average number of employees	Business income	Average business property
1	**2**	**3**	**4**
Micro	≤ 10	≤ 700.000 E	≤ 350.000 E
Small	> 10 ≤ 50	> 700.000 E ≤ 8.800.000 E	> 350.000 E ≤4.400.000 E
Medium-sized	> 50 ≤ 250	> 8.800.000 E ≤ 35.000.000 E	> 4.400.000 ≤ 17.500.000 E
Large	> 250	> 35.000.000 E	> 17.500.000 E

Full IFRS/IAS simplification was conducted to adjust to the SMEs' needs (group of authors, 2017). Regulations irrelevant to SMEs are eliminated, such as earnings per share, business segments, insurance contracts, etc. Simplifications are also issued for disclosure in different areas, including financial instruments, delayed tax assets and liabilities, employees' salaries, leasing, state benefits, etc. Intangible assets, real estate, plants, and equipment evaluation is also simplified.

For several reasons, special standards for SMEs are necessary (Sačer *et. al*, 2009). Financial institutions are lending internationally, so the banks rely on financial reports to decide on lending to these companies. Suppliers want to evaluate the financial health of the buyers in other countries before they deliver the goods or the appropriate services. Financial reports are the foundation for solvency rating by foreign credit rating agencies. Also, SMEs' capital moves across borders, so the financial reporting standardization of the sector is in their interest, and those of others who use their data.

All the countries that have completed the transition process encountered several problems during the transition to a market business model. Undeveloped corporate management with poor implementation of legal regulations makes many domestic companies risky for investment. Another weak point of corporate management in transitional economies can be recognized. Transparency and publication of reliable and relevant data are considered vital for efficient corporate management practice and market capital functioning. Although the legal regulation sets relatively high standards, the practice is frequently such that the public and even potential investors need more faith in the data published by the companies.

To establish a market-oriented economy, Serbia, like many other transitional countries, has faced numerous challenges in economic system creation, institution formation, and incentive establishment for economic performance improvement. In addition, corporate management is recognized as an essential factor for the development and improvement of the investment climate in the country. Although today Serbia has laws related to financial regulations, company registration, bankruptcies, taxes, duties, etc., the quality of economic legislation needs to be improved. Taking into account all the positive and negative effects, their implementation remains the main problem.

Considering the characteristics of the accounting legislation in the transitional period in Serbia, it still needs to inspire confidence that its application can achieve high-quality financial reporting and comparability at the international level. Specific activities that should be conducted with the aim of financial reporting harmonization are related to the following activities: normative and institutional framework upgrade; monitoring mechanism development; (3) market discipline functioning. Unlike the practice in economically developed countries, legislation in Serbia still has priority concerning professional accounting regulation.

The Law on Accounting and the Law on Auditing have been parallel in effect in Serbia since 2013 as two different laws, which is the first case in Europe. Also, there are no national accounting standards as in the case of 25 EU countries. Therefore, the business entities under no obligation to apply IAS/IFRS opt for IFRS for SMEs or the manual issued by the responsible Ministry. Domestic legislation harmonization with the EU 2013/34 guideline must be on time and implemented entirely.

METHODOLOGY

The research for this paper was conducted from September to December 2022 on a sample of 60 respondents, half of which were from large companies and the other half from SMEs. The division into small and medium-sized enterprises, on the one hand, and large companies, on the other hand, was conducted according to the current Law on Accounting of the Republic of Serbia. The structure of the respondents in the sample consisted of financial managers, accountants, and business executives. All the respondents had over three years of university degrees and work experience in accounting and finance.

The respondents evaluated the effect of the following factors on the financial reporting quality: personnel capability, management understanding, exit into the world market, domestic legislation, and IFRS harmonization. The responses were statistically processed in the SPSS program and tested by Cramer's test. The significance of the statistical differences between the responses from the two groups of companies was tested by the Chi-squared test.

Table 2. Sample structure in relation to the respondent's function and company size (crosstabulation)

Respondent's function	Company size	
	Large	Small and medium-sized
Accounting director	15	16
Manager	8	7
Finance director	7	7
Total	30	30

Table 3 shows that the most significant number of respondents from large companies (16) and SMEs (18) work in production.

Table 3. The structure of the sample in relation to the field the company comes from and company size (crosstabulation)

Field	Company size	
	Large	Small and medium
Production	16	18
Trade	14	12
Total	30	30

Descriptive indicators

Average mean values of personnel competence factor evaluation, management understanding, domestic legislation, and IFRS harmonization are more related to the theoretical average. In contrast, the factor of exit into foreign markets is lower concerning the theoretical mean values (Table 4).

Table 4. Factors' expressiveness

Factors	Theor. min.	Theor. max.	Empir. min.	Empir. max.	AS	SD
Personnel capability	1	5	1.00	5.00	3.233	1.198
Management understanding	1	5	1.00	5.00	3.550	1.111
Exit to the international market	1	5	1.00	5.00	2.833	1.304
Domestic legislation	1	5	1.00	5.00	3.017	1.282
IFRS harmonization	1	5	1.00	5.00	3.633	1.149

DISCUSSION ON THE RESEARCH RESULTS

Financial reporting quality increase through harmonization with international legislation causes direct and indirect benefits for each country. The immediate benefits are reflected in the national legislation developing into supranational, the international comparability of financial reports and audit findings, reduction of compliance costs with international factors, continuous professional improvement, current international legislation application, etc. Indirect benefits are reflected in foreign investment incentives, investment cost reduction, reducing the price of capital, financial market efficiency increase, providing the internalization of its economy, etc.

Small and medium-sized enterprises are increasingly founding their development on the internalization of their business, so the financial reporting harmonization process becomes a necessity. IFRS for SMEs is created to adjust to their needs, and it represents a modified version of standards for large companies and public entities. Positive effects on their financial performances are expected from SMEs' financial reporting harmonization, which is especially important for companies in transitional countries and their inclusion in the developed global market.

IFRS has been mandatory in Serbia since 2004 for banks and other financial organizations since 2003. Mandatory application of these standards is introduced with the aim of the accounting system harmonization with the generally accepted international standards. The problems accompanying the IFRS application in the transitional period are high inflation, exchange rate instability, frequent changes in legislation, the insufficient significance given to the IFRS application reflected in the lack of references dealing with the IFRS, delays in the translation of the standards, low level of representation in higher education, non-existent training and incentives by the state. The purchase value model is dominant in property, plant, and equipment evaluation, and the problem of insufficient professional evaluators in this field is also present.

Tax regulations often collide with accounting regulations which causes additional problems in the appropriate standard application. The competence of the people working on preparing and compiling financial reports needs to be legally defined, which often leaves some space for incompetent people to deal with this business, without proper certificates and licenses for the jobs, especially in SMEs and accounting agencies. These people justifiably ask questions about complex IFRS understanding, explanation, and application. Also, there is an additional problem of frequent legislation changes, and subordinate legislations need to be more compliant with it as well as IFRS. In this situation, internal accounting legislation and accounting policy creation has been done poorly.

Graph 1. Respondents' answers distribution in personnel capability factor evaluation considering the company size

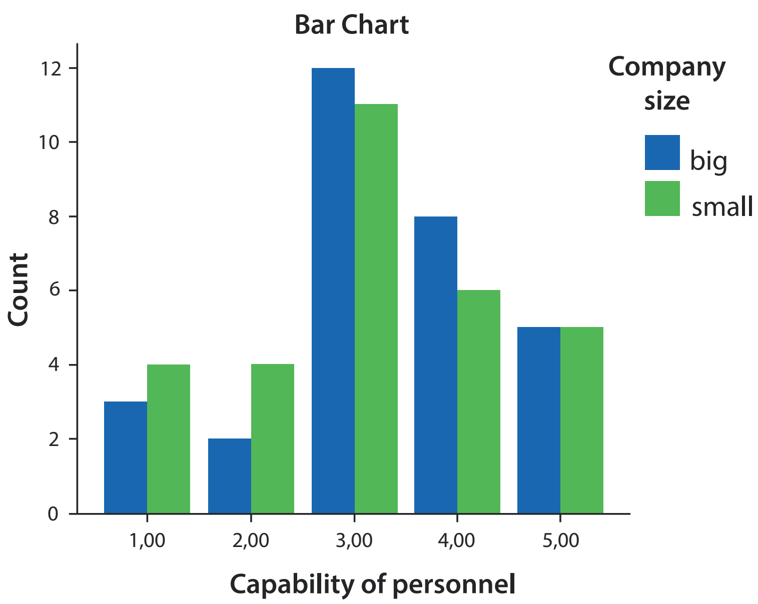

Table 5. Differences in respondents' responses to the personnel capability factor evaluation considering company size (X^2 test)

	Value	D. f.	Statistical significance
Pearson's X^2	1.139	4	0.888
Cramer's V	0.138		
Contingency coefficient C	0.136		

Source: *Author's research*

The respondents highly evaluated the personnel capability factor influence on financial reporting quality (graph 1, table 5). No statistically significant differences were established (X^2=1.139, p>0.05) in evaluating this factor considering company size, which indicates that SMEs pay a lot of attention to the people who do the bookkeeping and compile financial reports. Additionally, the Cramer's indicator is V=0.138, suggesting little connectivity between variables, which shows that the size of the organization has no bearing on how important staff competency is to the accuracy of financial reporting.

Company management is responsible for high-quality and transparent financial report compilation, which should present objective and comparable financial results and financial situation in a company in a certain period. Company management cares most about capital owners' positive reactions (shareholders, creditors). On the other hand, capital owners are dislocated in time and space, they do not have real insight into everyday business, and that is the reason for the management to make the right decisions in order to protect and increase their investments and capital. Therefore, financial reports that show the strongest and most profitable company, the finest outcomes for the organization, and efficient asset management are of particular importance to managers. In other words, they also want to demonstrate their skills.

Graph 2. The distribution of respondents' responses to management understanding factor evaluation considering company size

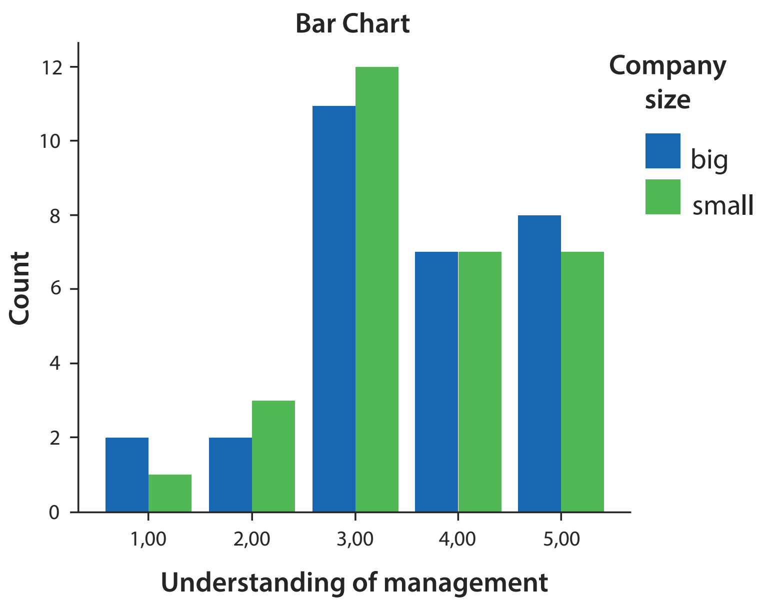

Table 6. The differences in management understanding factor considering company size (X^2 test)

	Value	D. f.	Statistical significance
Pearson's X^2	0.643	4	0.958
Cramer's V	0.104		
Contingency coefficient C	0.103		

***Source:** Author's research*

Research results show no statistically significant difference (X^2=0.643, p>0.05) in management understanding factor evaluation considering company size. Cramer's indicator is V= 0.104, which indicates low connectivity between the variables (graph 2, table 6). The result is significant for the SME sector because management's influence on financial reporting quality is highly evaluated, improving the companies' total business performances.

Accounting and financial reporting are increasingly globalized, with the increasing trade and investment scope among companies from various countries.These factors reinforce the need for quality financial reporting to become internationally comparable and consistent. Likewise, due to the increasing SMEs sector participation in the international market, there is a strong need for financial report harmonization, which should enable easier integration of these companies in the international market. Company capital moves across borders, and the reporting on company performances enables easier identification of the most productive use of capital, which makes the total resource allocation more efficient.

Graph 3. Respondents' responses distribution in the examination of the impact of company size on entry into the global market.

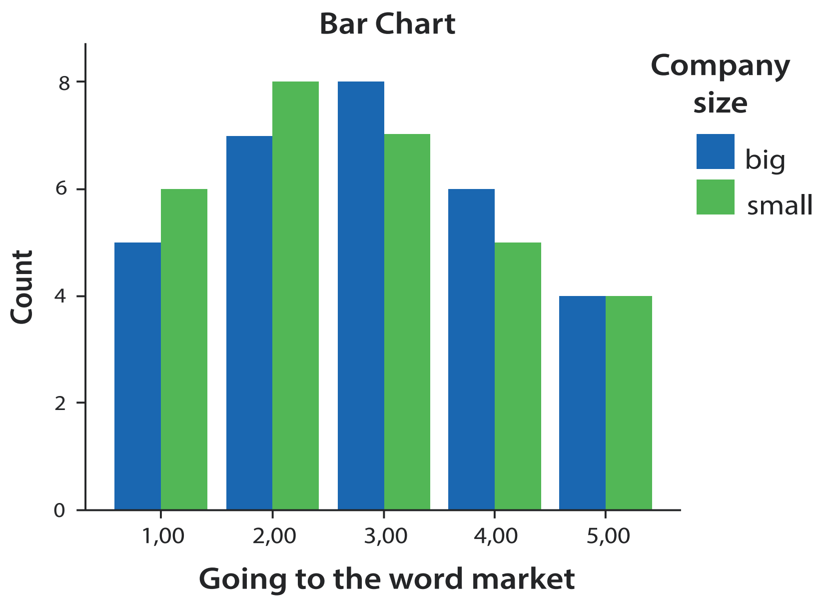

Table 7. Evaluation of the factors affecting company size related to variations in entry into the global market (X^2 test)

	Value	D. f.	Statistical significance
Pearson's X^2	0.315	4	0.989
Cramer's V	0.072		
Contingency coefficient C	0.072		

Source: *Author's research*

In examining the factor related to entry into the world market, the responses from major companies and the SME sector do not substantially differ from one another (X^2=0.315, p>0.05). Cramer's indicator is V=0.072, which indicates an insignificant connection between the variables (graph 2, table 7). This factor has a lower average score (AS=3), indicating that the companies, particularly the SME sector, consider that entry into the world market has a lower value than the other factors in the questionnaire.

Since 2013, Serbia has organized accounting in accordance with special auditing laws, making it the first instance of its kind in Europe. Also, there are no national accounting standards, as is in 25 EU countries. Legislation still needs to completely comply with EU Directive 2013/34. Frequent regulation changes, incompatible legal and subordinate legislation, as well as delayed translations, and the application of international standards are the characteristics of this period. The time between legislation adoption and application should be longer, which speaks of the need for more understanding of the regulatory bodies about the complexity of this issue. The essential changes in legislation often complicate the financial reporting process and reduce its quality.

Graph 4. Respondents' responses distribution in domestic legislation factor evaluation regarding company size

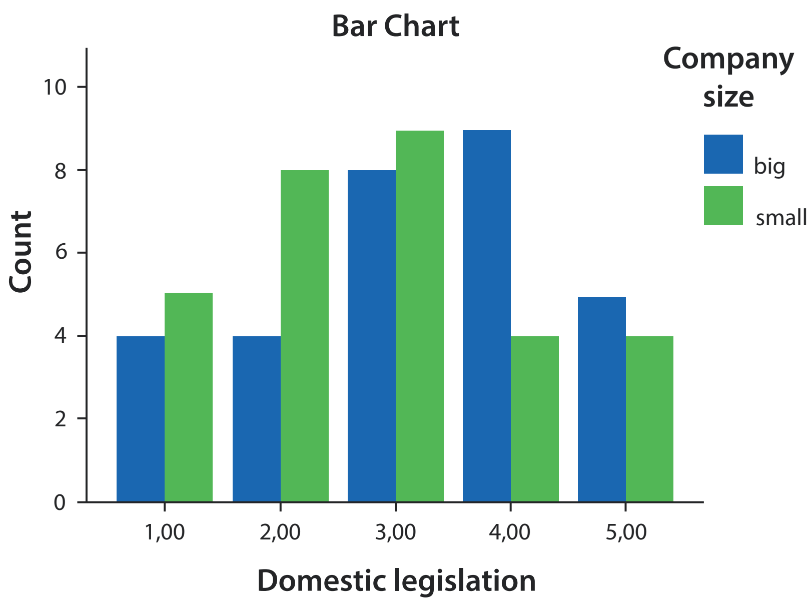

Table 8. The differences in domestic legislation factor evaluation regarding company size (X^2 test)

	Value	D. f.	Statistical significance
Pearson's X^2	3.537	4	0.472
Cramer's V	0.243		
Contingency coefficient C	0.236		

Source: *Author's research*

Research results of domestic legislation factor influence on financial reporting quality show that no statistically significant differences are established (X^2=3.537, p>0.05) in evaluating this factor regarding the company size. Also, Cramer's indicator (V=0.243) indicates low connectivity between the variables. The companies evaluate this factor similarly, regardless of the company size (graph 4, table 8).

Although the process of IFRS adoption and application in the EU has started in 2005, there are differences in harmonization levels from country to country. The most important factors initiating these differences are the character of the legal system, the way of economy funding, the relation between financial and tax accounting, the accounting profession status, and the degree of accounting theory development (Eliot, B., Eliot, J., 2011). Financial reporting harmonization is a long-lasting process that requires the cooperation of the state and its authorities, professional organizations, the accounting profession, management, and a broad public because of the financial reporting character of public interest. In Serbia, the cooperation of the state and its authorities with the other participants in harmonization needs to be improved, which is reflected in numerous problems in everyday business and the relation to the state institutions (Ministry of Finance, Tax Administration, etc.).

Graph 5. Respondents' responses distribution on IFRS harmonization factor evaluation regarding company size

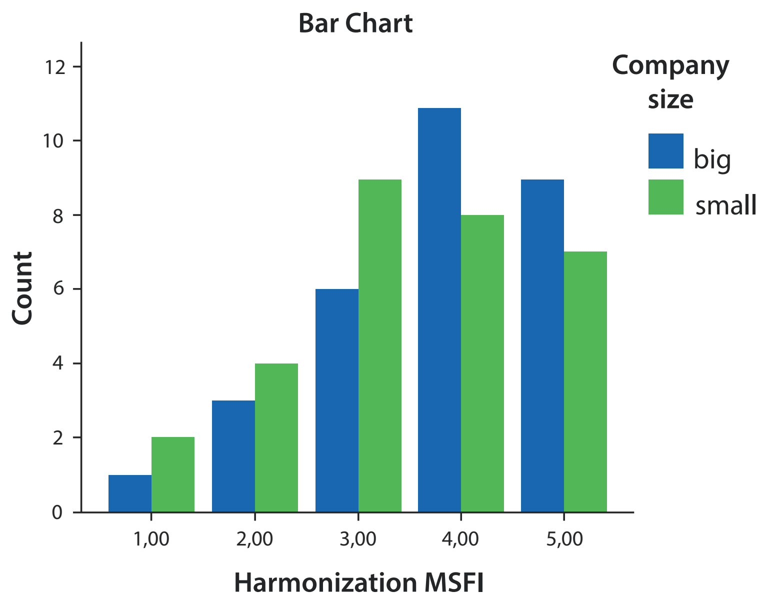

Table 9. The differences in IFRS harmonization factor evaluation regarding company size (X^2 test)

	Value	D. f.	Statistical significance
Pearson's X^2	1.800	4	0.773
Cramer's V	0.173		
Contingency coefficient C	0.171		

Source: *Author's research*

The results show no statistically significant differences (X^2=1.800, p>0.05) in IFRS harmonization factor evaluation regarding company size. Cramer's indicator is V=0.173, which indicates a low correlation between the variables, and it means that all the companies, regardless of size, give this factor a great deal of significance (graph 5, table 9). The SMEs sector attaches great importance to this factor, which will positively impact the possible internalization of the company's business dealings.

RECOMENDATIONS AND CONCLUSIONS

Nowadays, financial reports are the primary source of information for shareholders, creditors, employees, business partners, management, and other interest groups. They enable us to look at property movement, liabilities, capital, cash flows, costs, income, profitability, financial structure, and other important information about the company. Financial reports present the results achieved in the previous period, but they are also the starting point for the development of reliable evaluations on the company's perspective and future performances. Reporting on company performances makes it easier to identify the areas of the most productive capital usage and more efficient resource allocation in the entire market.

The international standards of financial reporting are the standardization instruments at the global level facilitating international communication. The country that provides quality accounting reporting according to the IAS/IFRS gains the following advantages: increases its own abilities to take part in the global capital market, encourages capital inflow, simplifies reporting demands, simplifies international comparison possibilities, reduces the cost of quality financial reporting demand adaptation and the necessity of their continuous improvement, encourages capital market access around the world and directly increases the efficiency of its own securities market, etc.

Modern companies are becoming multinational, and trade and investment scope between companies from different countries is increasing. It causes the need for internationally comparable and consistent quality financial reporting. The financial reports' accounting information serves as the current situation's information and business language of communication. As such, it should be harmonized so that all the participants can cooperate and communicate without interference in the global market. Financial reporting harmonization is essential for all large businesses, but it is also important for the SME sector, which is trying to ensure its business growth by entering the global market.

National accounting legislation harmonization with international standards is essential for countries in transition where foreign capital is necessary for rapid economic development. IFRS has been mandatory in Serbia since 2004 for banks and other financial organizations since 2003. The biggest problems in IFRS application in the transitional period are high inflation, exchange rate instability, frequent legislation changes, dominant purchase value model application (neglected fair value model), underdeveloped securities market, the insufficient significance given to IFRS application reflected in the lack of references on the IFRS, delay in IAS/IFRS translation, poor representation in higher education, non-existent training and state incentives, etc.

The research conducted in this paper has confirmed several shortcomings and limitations in standardized financial reporting in Serbia. Accounting is regulated by a special law in the field of audit, which is a precedent in Europe. There are no national standards, although they exist in 25 EU countries. Legislation is still not fully compliant with the 2013/34 EU Directive. Legislation often has priority over professional accounting regulation, especially when it comes to problems with tax aspects. The companies are forced to perform the appropriate business changes and decisions based on the interpretation of the Ministry of Finance and Tax Administration, regardless of their competence degree and IAS/IFRS knowledge.

The respondents have confirmed that the subordinate legislation is often incompatible with legal and international regulations, with frequent regulatory changes and delays in translation and, therefore, the implementation of international standards. The time between legislation adoption and implementation is often very short, which concerns the regulatory bodies' need to understand the issue's complexity.

The essential regulatory changes often unnecessarily complicate the financial reporting process, reducing its quality at the same time.

Serbia has other characteristics – the competence of the people preparing and composing financial reports is not determined by law, which leaves a lot of space for incompetent people to do the job, without appropriate certificates or licenses, particularly in SMEs and accounting agencies. It is undisputed that this regulator's failure influences financial reporting quality and delays the harmonization process with the international standards because these people cannot completely understand, interpret and implement the complex IFRS. Also, it negatively influences internal accounting regulation quality and accounting policy implemented by the companies.

Serbia needs much more participation of the accounting profession in legal and subordinate regulation adoption. It would help avoid many problems in financial reporting practice, the cause of which is regulation adoption without consulting the profession. Legal and subordinate regulations should be specific in order to prevent ex-post interpretations by state institutions. It would also reduce frequent subordinate legislation changes, often performed shortly before or during financial report preparation. Tax balances are made on the basis of the financial reports, so all the inaccuracies in financial reporting are reflected in the tax liabilities calculations' accuracy. In addition, specific legislation leaves less room for creative' accounting and a grey economy widespread in Serbia, as unfair competition to the legal economy, especially the SME sector.

Because of all the, it is necessary to introduce mandatory professional certification for the people responsible for financial report compilation in Serbia by the internationally recognized professional organization. This would improve professional status because only qualified people would do these jobs, and they would invest in improving their knowledge afterward. Accountants' practical education and improvement should be more emphasized, and thus more qualified people would be available for these jobs, raising the financial reporting ethical codex to a higher level. These measures would have a positive effect, especially for SMEs, where the accounting profession is frequently considered through the prism of meeting legal regulations in bookkeeping and report submission for the state institutions' needs.

Management is responsible for financial reporting quality in a company and therefore its role is of considerable significance in the process. The management decides on the choice, evaluation and use of the accounting methods, as well as the level of financial reporting additional information disclosure. It is certain that the management's understanding of the financial report's essence and purpose will significantly contribute to the accounting information's usefulness and financial reporting quality. This approach will be recognized in the long run in both domestic and international markets, with the appropriate benefits for the company.

The research in this paper shows that small and medium-sized enterprises have evaluated the factors influencing financial reporting quality in Serbia similarly to large companies. Therefore, the research results are particularly encouraging because they prove that the SME sector understands the necessity of harmonization of financial reporting standards, domestic legislation improvement, and the significance of these processes for the company growth through the increase in the possibility of entry into the international markets. On the other hand, it will also positively influence the development of the profession and the status of the people responsible for bookkeeping and financial report compilation.

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KVALITET FINANSIJSKOG IZVEŠTAVANJA U FUNKCIJI RASTA PREDUZEĆA U SRBIJI

Rezime:

Razvoj računovodstvene profesije i kvaliteta finansijskog izveštavanja kreće se uporedo sa razvojem tržišne privrede što doprinosi stabilnosti finansijskog sistema i podiže efikasnost tržišta kapitala i privrede u celini. U ovom radu se istražuje uticaj pojedinih faktora na podizanje kvaliteta finansijskog izveštavanja u Srbiji. Cilj rada je da identifikuje ograničenja i probleme u primeni MRS/MSFI, utvrdi dejstvo faktora koji imaju najveći uticaj na ovaj proces i preporuči predloge rešenja nadležnim državnim institucijama za uspostavljanje sistema kvalitetnog finansijskog izveštavanja koje će značajno pomoći razvoju i podizanju medjunarodne konkurentnosti domaćih prreduzeća. Rezultati sprovedenog empirijskog istraživanja su pokazali brojne slabosti u sistemu finansijskog izveštavanja u Republici Srbiji koje se ogledaju u čestim izmenama zakonske regulative, malom učešću računovodstvene profesije u donošenju zakonskih propisa, često selektivnoj primeni MSFI, nepostojanju nacionalnih računovodstvenih standarda, nedovoljnom praktičnom obrazovanju i usavršavanju računovodstvenih kadrova, neuskladjenoj Zakonskoj regulativi sa Direktivom EU 2013/34EU i dr. Zbog toga su na kraju rada date preporuke nadležnim institucijama u Republici Srbiji kako bi se oblast finansijskog izveštavanja unapredila i osavremenila, što bi sa svoje strane uticalo na bolje preformanse preduzeća na domaćem i medjunarodnom tržištu.

Ključne reči:

finansijsko izveštavanje,
međunarodni standardi,
kompanija,
Srbija.