The Implementation of GAPSME by Maltese Companies: An Analysis

By

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May 2019

19MACC079

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ABSTRACT

The Implementation of GAPSME by Maltese Companies – An Analysis

PURPOSE: This study has three distinct research objectives. The first objective is to determine the GAPSME take-up rate three years after its issuance. The investigation of factors which influence a Maltese SME's financial reporting framework choice is set as the second objective, while the third objective is to gauge the feedback and opinion relating to GAPSME's use in practice by both auditors and SME representatives.

DESIGN: A mixed method methodology comprising of both quantitative and qualitative aspects was the approach adopted which was deemed to provide the most comprehensive study which satisfies the research objectives stated above. Data gathered through company financial statements was statistically analysed through a binary logistic regression and supplementary statistical testing, while semi-structured interviews provided an insight into stakeholder reasoning and opinions which was used to support and discuss the quantitative findings.

FINDINGS: This study identified a GAPSME take-up of 82.4% in its first year of issuance, which was found to be much higher than GAPSE's take-up in its final year of availability (2015), which was approximately 50%. The factors which were found to influence whether firms are GAPSME adopters or not included: company size, auditor size, increases in audit fees pre and post GAPSME issuance, auditor report lag, use of GAPSE in the past, investment in subsidiaries and the company's debt/equity ratio. Overall feedback from both sets of interviewees was positive, with many only recommending some improvements in relation to simpler recognition and measurement principles and higher small group consolidation thresholds. GAPSME was not considered inferior to IFRSs for its targeted users, which contrasted to perceptions of its predecessor. The banks' reliance on financial statement information was found to be a misconception, while SME owners and creditors were not considered avid users of audited financial statements. Lastly, transitional costs due to GAPSME adoption were minimal, while indirect cost saving through no change in audit fees was experienced when compared to the ever more complex IFRSs.

CONCLUSIONS: This study concludes that GAPSME can be considered a success, visible through its high take-up and general feedback, however improvements addressing stakeholder concerns should be considered by the MIA. The company factors which effect an SME's framework choice provide insight into which companies are more likely to adopt GAPSME and therefore at which such improvements should be targeted.

VALUE: The strength of this study lies in the fact that it is the first feedback study on GAPSME since its use in practice and the first to investigate relationships between company specific factors and framework choice.

KEYWORDS: GAPSME, Differential reporting, SME Framework choice.

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This dissertation is dedicated to my parents, Joanne and Charles Sciriha, who through their constant love and support have made all my academic achievements possible.

AKNOWLEDGMENTS

I would like to take this opportunity to thank everyone who directly or indirectly assisted me during the preparation of this dissertation.

Firstly, my sincere gratitude goes to my dissertation supervisor, Mr Frank Cassar, B. Accountancy. (Hons), M.I.A, C.P.A. for his guidance throughout the carrying out of this dissertation. His dedication and expertise together with valuable life lessons have been inspiring and valuable to the completion of this study and my own personal development.

I am also grateful to Ms Lara E. Pace, B.Sc. (Hons) Maths, Statistics & Operations Research, M.Sc. (Statistics) for her assistance with the statistical analysis of this study and her constant advice and correspondence throughout this research.

I would also like to acknowledge and thank the staff at the Registry of Companies for being so helpful and welcoming, as well as the auditor and SME interviewees for contributing their time, knowledge and experience by accepting to be interviewed. Their cooperation was crucial for the completion of this dissertation.

My deepest thanks go to my dearest parents, Joanne and Charles, family members and close friends, for their constant support throughout all my years of study. I also express my sincere appreciation to my girlfriend, Rebecca, for always being by my side and her continuous support and belief in me.

Finally, I would like to thank God for granting me the strength and health to carry out and achieve my academic goals.

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LIST OF ABBREVIATIONS

AB	Accountancy Board
ACCA	Association of Chartered Certified Accountants
AcSB	Accounting Standards Board (Canada)
AICPA	American Institute of Certified Public Accountants
ASB	Accounting Standards Board
ASCG	Accounting Standards Committee of Germany
ASCS	Accounting standards Council of Singapore
BIS	Department for Business Innovation and Skills
CA	Companies Act
CICA	Canadian Institute of Chartered Accountants
EC	European Commission
ED	Exposure Draft
EU	European Union
FAF	Financial Accounting Federation
FASB	Financial Accounting Standards Board
FRC	Financial Reporting Council
FRCN	Financial Reporting Council of Nigeria
FRSSE	Financial Reporting Standards for Small Entities
GAAP	Generally Accepted Accounting Principles
GAPSE	General Accounting Principles for Small Entities
GAPSME	General Accounting Principles for Small and Medium Enterprises
IASB	International Accounting Standards Board

IASs	International Accounting Standards
ICANZ	Institute of Chartered Accountants of New Zealand
IS	Income Statement
IFRSs	International Financial Reporting Standards
LIFO	Last-In-First-Out
MACM	Malta Association of Credit Management
MFSA	Malta Financial Services Authority
MIA	Malta Institute of Accountants
PIEs	Public Interest Entities
ROC	Registrar of Companies
SAD	Single Accounting Directive
SIA	Swaziland Institute of Accountants
SMEs	Small and Medium Enterprises
SMPs	Small and Medium Practitioners
SOCF	Statement of Cashflows
SOCIE	Statement of Changes in Equity
SOFP	Statement of Financial Position
UK	United Kingdom
USA	United States of America

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Chapter 1

Introduction

1.1 – INTRODUCTION

This chapter will give an introduction and add context to the study through relevant background information, the reasoning behind its necessity, this dissertation's research objectives, scope and limitations.

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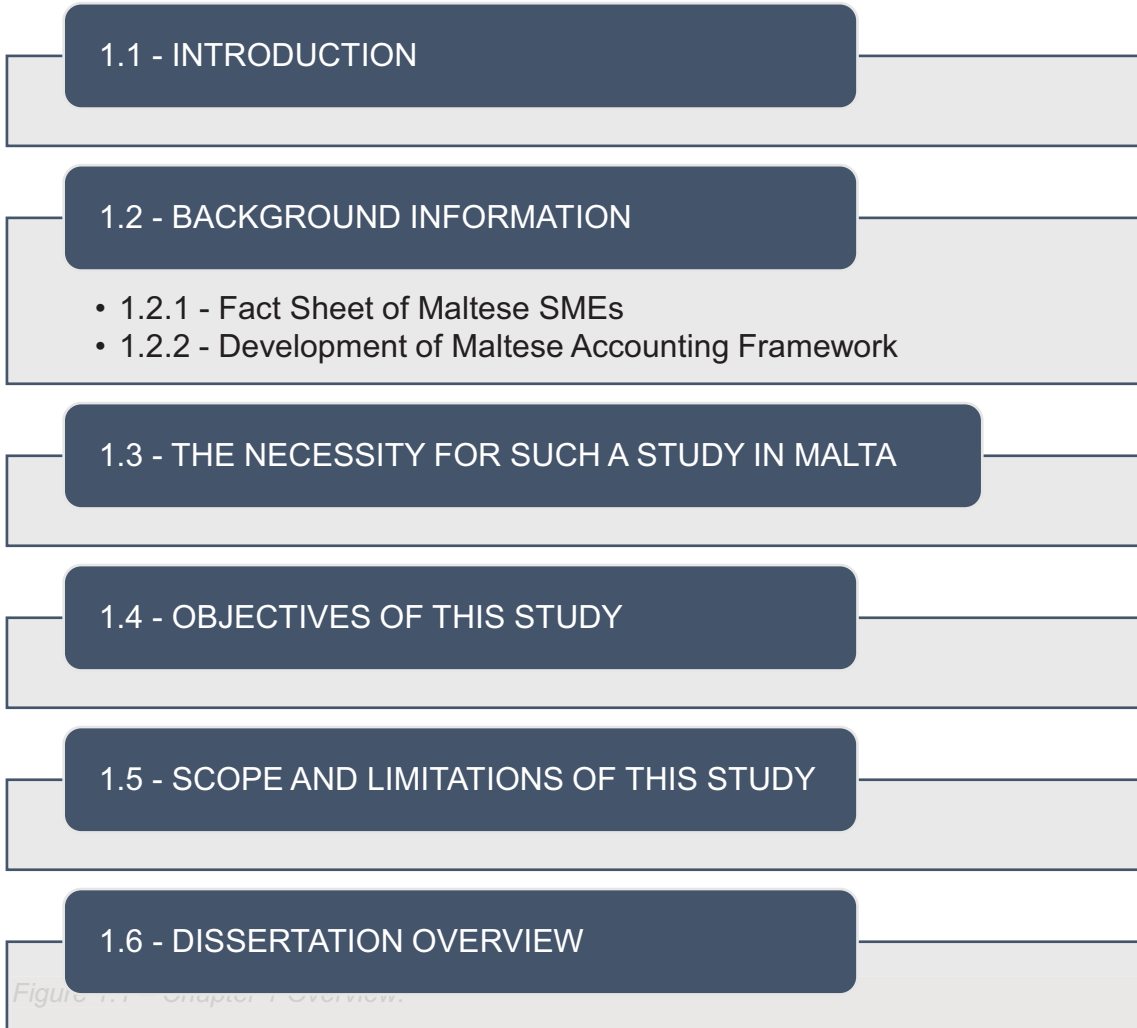
Figure 1.1 – Chapter 1 Overview.

1.2 - BACKGROUND INFORMATION

1.2.1 – Fact Sheet of Maltese SMEs

Small and Medium Enterprises (SMEs) account for 99.8% of the share of enterprises in Malta, which is highly comparable to the European Union (EU) Average figure. SMEs employ a substantial 80.9% of the Maltese private sector, which in turn is higher than the percentage evidenced in the EU-wide statistic (66.4%) (SBA Fact Sheet, 2018). To top it all, 81% of all value added is derived from the aforementioned companies in Malta, which further illustrates the vital importance SMEs have on the Maltese economy (SBA Fact Sheet, 2018).

Class Size	Number of enterprises		Number of persons employed		Value added	
	Malta	EU-28	Malta	EU-28	Malta	EU-28
Micro	92.4%	93.1%	33.3%	29.4%	37.0%	20.7%
Small	6.3%	5.8%	25.0%	20.0%	25.5%	17.8%
Medium	1.1%	0.9%	22.6%	17.0%	18.5%	18.3%
SMEs	99.8%	99.8%	80.9%	66.4%	81.0%	56.8%
Large	0.2%	0.2%	19.1%	33.6%	19.0%	43.2%
Total	100%	100%	100%	100%	100%	100%

Table 1.1 – Size demographics in Malta and across the EU. Source: SBA Fact sheet - Malta, 2018, pp.2.

1.2.2 – Development of Maltese Accounting Frameworks

The Companies Act (CA) of 1995 (Chapter 386 of the laws of Malta) stated that all companies, irrespective of their size, had to prepare their financial statements in accordance with International Accounting Standards (IASs) issued by the International Accounting Standards Board (IASB). Historically, this was considered to be an advantage, as any imposition by the EU on its member states to adopt IASs will never create major transitional shockwaves in the Maltese

profession. This resilience would have allowed the local profession to progress at a faster pace (Hon. T.Fenech, 2004).

However, from the turn of the century, the IASB started issuing a new raft of financial standards which changed the dynamics of how the Maltese profession viewed International Financial Reporting Standards (IFRSs). This is best described by an extract from the comment letter submitted to the IASB by the Malta Institute of Accountants (MIA).

> "In Malta, all companies regulated by the Companies Act, 1995 ('the Act') have a statutory obligation to prepare financial statements that conform with International Financial Reporting Standards (IFRS). The great majority of those entities (over 95%) are SMEs – no matter how one might define 'small' or 'medium-sized'. Practical compliance with IFRS has become increasingly burdensome for Maltese companies with the increasing 'sophistication' of IFRS, including in particular, the onset of IAS 39 on Financial Instruments."
>
> (MIA, 2004, pp. 1)

This proved to be the first seed sown relating to differential reporting in the local profession. Differential reporting is all about creating different frameworks, each of which are adapted to the specific needs and size of companies which fall within that particular entity category (Collis and Jarvis, 2003).

The IASB's chosen course of action was to issue the IFRS for SMEs framework, however the MIA was not convinced that such a framework was simple enough to be adequate and optimal for Malta. In view of this, the MIA, based on the request by the Accountancy Board (AB), decided to develop its own financial reporting framework. Such a framework was based on a mixture of principles derived from IFRSs, the 4th EU directive and the Financial Reporting Standards for Small Entities (FRSSE) (Alexander and Micallef, 2011). This framework, called GAPSE, was issued in February 2009, making it the first time that Malta had a two-tier financial reporting system, with IFRSs as adopted by the EU being the default Generally Accepted Accounting Principles (GAAP) and GAPSE being the optional alternative to qualifying entities (Alexander and Micallef, 2011).

In spite of all this, GAPSE's take-up by companies was unexpectedly low, with only 18.5% of eligible SMEs applying the framework (Zammit, 2011). Zammit (2011) also identified possible reasons why such a low GAPSE utilisation rate was observed:

- Lack of awareness and knowledge relating to GAPSE and its benefits;
- SMEs part of a group of companies preferred IFRSs due to enhanced comparability;
- IFRSs were considered more adequate for SME reporting requirements; and
- GAPSE being mainly beneficial for larger SMEs rather than the more numerous micro entities.

Faced with such an incumbent situation, the AB took the opportunity to further update the financial reporting framework by jumping on the bandwagon of the transposition of the Directive 2013/34/EU, more commonly known as the Single Accounting Directive (SAD), into Maltese legislation. This culminated in a revamped GAPSE through a newer version called General Accounting Principles for Small and Medium Enterprises (GAPSME), which had its quantitative thresholds aligned with the lowest possible member state option provided through the aforementioned EU directive. Notably, large companies and Public Interest Entities (PIEs) were obliged to use IFRSs as adopted by the EU, which implies thresholds of the qualitative nature were also used.

	Small	Medium
Balance sheet total	≤ €4,000,000	≤ €20,000,000
Revenue	≤ €8,000,000	≤ €40,000,000
Average number of employees	≤ 50	≤ 250

Table 1.2 – GAPSME individual firm size thresholds. Source: Delia and Spiteri Bailey, 2016, The Accountant, pp.1.

This meant that GAPSME is now the default accounting framework for SMEs and is officially applicable for financial reporting periods commencing on or after 1ˢᵗ January 2016 (Accountancy Profession Act CAP 281, LN 289, 2015). The GAPSME thresholds, as seen in Table 1.2, have a broader reach when compared the more restrictive GAPSE thresholds (Article 5 of Legal Notice 51, 2009).

Disclosure and presentation requirements were also drastically reduced. Table 1.3 shows the GAPSME presentation requirements for small and medium companies.

Small Entity Presentation Requirements	Medium Entity Presentation Requirements
Statement of Financial Position	Statement of Financial Position
Income Statement	Income Statement
Limited notes	Full notes
	Statement of Change in Equity
	Statement of Cash flows

Table 1.3 - GAPSME presentation requirements for Small and Medium Enterprises. Source: Accountancy Profession Act CAP 281, LN 289, 2015, pp. B2909.

The reporting burden for small companies using GAPSME was therefore significantly reduced when compared to the previous GAPSE and medium company requirements. However, these additional simplifications also brought about certain disadvantages to firms.

The abolishment of the Statement of Cashflows (SOCF) requirement was deemed a step backwards, as such a statement is considered especially relevant to SMEs, particularly relating to their access to external finance (Abela, 2014). Several stakeholders such as banks, investors and creditors expressed their need for more information which could cause a potential problem for SMEs aiming to obtain essential external financing (Abela, 2014). Other downsides of GAPSME include the lack of comparability between Maltese SMEs and other firms together with the expected transitional workload suffered by the accountancy profession in GAPSME's earlier years (Dimech, 2016).

1.3 – THE NECESSITY FOR SUCH A STUDY IN MALTA

A study directly looking into the take-up rate and a structured feedback exercise in relation to the recently issued GAPSME accounting framework is yet to be carried out. A plausible reason why this has not been done yet would be the fact that it was only recently implemented in 2016 and therefore not an adequate amount of time would have elapsed to derive the necessary findings.

Such a study was also recommended by several dissertations, such as Bugeja (2017), Dimech (2016) and Abela (2014), with which findings gathered through this study will be compared enabling further analysis. A similar research exercise was conducted by Zammit (2011) relating to the then newly developed General Accounting Principles for Small Entities (GAPSE) framework. Comparisons with this study will further provide insight into differences between GAPSME and its predecessor.

Three years down the line, one would expect the transitional period to have mostly taken place and therefore a dissection of the wide use of GAPSME and feedback on how the GAPSME framework has fared in practice can be obtained.

It would be interesting to see whether GAPSME, with its broader application through its more flexible thresholds and further simplifications has proven to be a preferred option and is considered a more appropriate framework to be used by SMEs in comparison to its former counterpart GAPSE and the alternative option, being IFRS as adopted by the EU.

In addition to this, no studies delving into the relationship between company specific factors and a company's accounting framework choice were found. The second research objective of this study will therefore strive to address such a research gap, with specific reference to the Maltese scenario.

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To summarise, this thesis will take a comprehensive look at the GAPSME framework in practice and seek to analyse any potential downfalls and improvements in order to improve financial reporting in Malta. Company specific factors effecting the framework choice will also be identified, providing further information and understanding of relationships which may improve GAPSME as a framework which truly has SMEs' best interest at heart.

1.4 – OBJECTIVES OF THIS STUDY

1) Assess the take-up of GAPSME by eligible Maltese SMEs.
2) Assess whether specific company's factors have an impact on the accounting framework applied by SMEs (GAPSME vs IFRSs as adopted by the EU).
3) Obtain feedback by auditors and SMEs regarding GAPSME, together with suggested improvements and their opinions on the framework 3 years after its issuance.

1.5 – SCOPE AND LIMITATIONS OF THE STUDY

The majority of quantitative data collected pertained to the companies' 2016 financial statements. While this was the most recent year for which all sampled companies had filed their financial statements with the Registrar of Companies (ROC), as most 2017 financial statements were not yet available publicly at the time of this study, 2016 financial statements were also the first financial statements which could be prepared under GAPSME. This therefore indicates that the quantitative data is mainly a snapshot of one year's (2016) financial statement figures.

As the ROC does not categorise companies according to size, the sample of companies had to be chosen from a population containing all company sizes and

not purely SMEs. This population also included companies which have since been dissolved.

The qualitative portion of the study represents the opinion of interviewees as at April 2019 whilst the quantitative data is a snapshot of figures as at 2016. This means that the timeframes of both data types could not be aligned.

The scope of this study does not include feedback on GAPSME by all users of SME financial statements but is limited to auditors and SME representatives.

1.6 – DISSERTATION OVERVIEW

Figure 1.2 visually illustrates this study's structure, segmented into 5 main chapters. While the introduction included general information about the study, Chapter 2 will give a comprehensive look of literature relating to this study, Chapter 3 will explain in detail the methodology used in executing this research, Chapter 4 will list all relevant findings obtained in relation to the research objectives of this study while also analysing and discussing such findings while Chapter 5 will summarise such findings and deduce recommendations and further areas of research.

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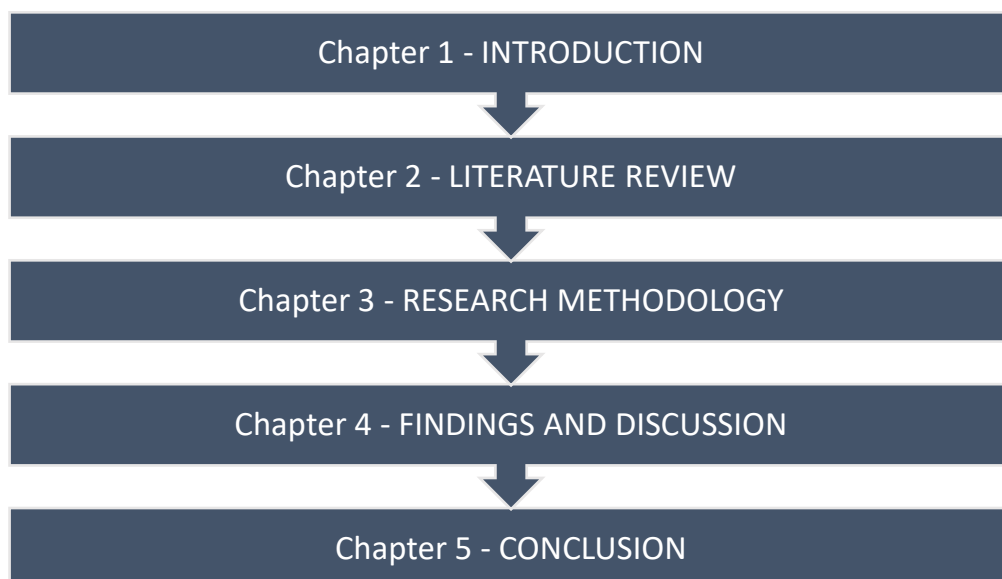
Figure 1.2 - Dissertation Overview.

Chapter 2

Literature Review

2.1 – INTRODUCTION

This chapter will feature an in-depth and comprehensive review of relevant international and local literature relevant to this study. A detailed illustration of how this chapter is structured can be observed in Figure 2.1.

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Figure 2.1 – Chapter 2 Overview.

2.2 - DIFFERENTIAL REPORTING DEFINITION

A good starting point is to introduce what differential reporting is. The Accounting Standards Council of Singapore (ASCS) defines differential reporting as:

> "the notion that some entities should be allowed to depart from particular requirements of accounting standards or entire accounting standards in preparing their financial statements."

(ASCS, 2008, pp.1)

In simpler terms, differential reporting is the concept that companies grouped in homogenous categories should be subject to different financial reporting requirements more suitable to their particular characteristics (Collis et al., 2001 as cited in Collis and Jarvis, 2003).

2.3 – PROS AND CONS OF DIFFERENTIAL REPORTING

2.3.1 - Main arguments highlighting the need for differential reporting

Accounting regulation has historically been developed to accommodate the needs of large listed entities. The IASB is also guilty of such bias, as IFRSs are clearly targeted towards large entities which are players in international capital markets (IASB, 2007 as cited in Rossouw and Van Wyk, 2009). This therefore suggests that the needs of SMEs have been unjustly ignored, especially since they contribute so significantly to the global economy (Coetzee, 2007).

Due to this disregard of specific needs, SMEs have had to put up with a significant cost and reporting burden in order to prepare their financial statements in accordance to full IFRSs (Cleminson and Rabin, 2002 as cited in Rossouw and Van Wyk, 2009). This sentiment was commonly stated in country-specific studies related to the views towards differential reporting.

Examples of such studies include those carried out in:

- Romania (Bunea et al., 2012)
- United States (AICPA, 1983 as cited in Knutson and Wichmann, 1985)
- Canada (Maingot and Zeghal, 2006 as cited in Stainbank and Wells, 2007)
- Nigeria (Ezeagba, 2017)

A study conducted by the IASB found that 24 of 30 national regulators expressed the need for simplified disclosure, recognition and measurement regulations (Pacter, 2004 as cited in IFAC, 2006).

2.3.2 - Main disadvantages of full IFRSs

2.3.2.1 – Over-complexity

IFRSs are often regarded as too bulky, theoretical, difficult to comprehend and implement (Topazio, 2007). This is amplified by the inherent characteristics of smaller companies which make it harder for such entities to comply with the comprehensiveness required by full IFRS financial statements (Archie and Elishia Rufaro, 2008).

Such characteristics include:

- Low number of employees (Archie and Elishia Rufaro, 2008)
- Limited financial expertise (Marriott and Marriott, 2000 as cited in Che Ku Hisam et al., 2017)
- Lack of resources, such as an up-to-date computerised system (Breen et al., 2003 as cited in Che Ku Hisam et al., 2017)

2.3.2.2 – Cost

The above characteristics result in the undesirable situation where costs of producing financial statements outweigh the benefits gained by SMEs (Boymal, 2006 as cited in Koppeschaar, 2012). Costs associated with the production of financial statements are not comprised only of financial costs, as there could be

potential costs of disclosing detailed information to competitors, which is amplified when full IFRSs are adhered to (Bunea et al., 2012).

2.3.2.3 - Irrelevant information to users

Not only are IFRSs not deemed suitable for SMEs themselves, but also for SME financial information users, many of which are not considered to be professional users and therefore find it challenging to extract the relevant information from the technical nature of IFRS accounts (Rossouw and Wyk, 2009). The resulting inaccurate, unreliable and irrelevant information provided by SMEs may even hinder their chances of gaining vital external finance, and therefore threaten their existence altogether (Amidu et al., 2011).

The importance of such complex financial statements for SMEs is also weakened due to the fact that the main users of such financial statements are mainly banks, tax authorities and the owners themselves, which all have access or may demand access to additional information at will (Hattingh, 2001 as cited in Rossouw and Van Wyk, 2009).

There is however a severe lack of literature and studies looking into the needs of SME users (Schiebel, 2008). Other studies also concluded that a financial reporting framework which is aimed specifically at SMEs should firstly aim to target their users' needs (McAleese, 2001:18 as cited in Rossouw and Van Wyk, 2009).

Considering the above arguments, several countries set upon developing their own differential reporting frameworks (Rossouw and Wyk, 2009). Furthermore, the IASB also recognised the need to address these problems and embarked on a project to produce an international financial framework aimed at mitigating SME concerns. This culminated in the issuance of the exposure draft (ED) of IFRS for SMEs in 2007 (IASB, 2007).

2.3.3 - Arguments against differential reporting

There is also considerable opposition to the concept of differential reporting. This may be due to the suboptimal implementation of the different accounting frameworks by various jurisdictions (IFRS, 2007).

The need for international accounting stems from several factors including the financial reporting scandals which took place in recent times and the rise to power of the European and Asian markets which initially operated under different accounting standards. Facilitating the needs of the global market spurred the development of IFRSs (Alami and Ouezzani, 2014).

The IASB's goal through such projects was to provide international stakeholders with relatively homogenous information with enhanced reliance and comparability. According to Mhedhbi and Zeghal (2006), this provided improvements in the following areas:

2.3.3.1 - Capital and investment flows contributing to economic development

International frameworks were considered especially helpful for developing countries in speeding up economic growth. Empirical evidence from Zimbabwe (Chamisa, 2000) and Albania (Fino, 2009) confirm this effect. Baldarelli et al. (2012) also found that international harmonisation of financial reporting would lead to a lower cost of capital which in turn is expected to cause an increase in investment.

2.3.3.2 - Information credibility

Baldarelli et al. (2012) state that harmonisation will improve the quality of the financial information produced. Furthermore, Nair and Rittenberg (1982 as cited in Knutson and Wichmann, 1985) suggested that different user needs are a "belief on behalf of businessmen and CPAs" and that users, especially banks, will always prefer having more information rather than less.

Another article also shows that the Financial Accounting Standards Board (FASB) would go as far as admitting that there may be a legitimacy towards the

reduction in disclosures in some cases, but recognition and measurement simplifications were considered useless towards reducing the burden on SMEs, as this would only contribute to diluting the effectiveness of financial statements (Ernst and Whinney, 1984 as cited in Knutson and Wichmann, 1985).

2.4 – IS A LOCALLY DEVELOPED GAAP WORTH IT'S SALT?

As discussed in the latter paragraphs of the previous section, one can deduce that IFRSs are expected to provide higher quality information, which is more relevant and useful, when compared to locally developed GAAP. This hypothesis has been both discarded and confirmed in the fairing findings across various studies.

Studies in Germany suggest that IASs did not directly correlate to:

- Improvements in earnings management (Van Tendeloo and Vanstraelen, 2005 as cited in Barth et al. 2008)
- Reductions in cost of capital (Daske, 2006 as cited in Barth et al. 2008)
- Differences in value relevance (Hung and Subramanyam, 2007)

Similar results were observed in China, as value relevance reportedly declined for domestic firms using IASs when compared to Chinese GAAP (Eccher and Healy, 2003 as cited in Barth et al., 2008).

Some explanations for the above include the fact that some countries do not possess the necessary infrastructure and resources to be able to enforce IAS regulation. This may therefore result in IAS benefits not being exploited due to the standards not being adhered to as intended (Eccher and Healy, 2003 as cited in Barth et al., 2008).

National attempts to create a differential reporting framework do however have their disadvantages such as these standards still referring to frameworks such as IFRSs. Peter Langard, ex Accounting Standard Board (ASB) and Association of Chartered Certified Accountants (ACCA) President, suggested that unless the

ASB made FRSSE a stand-alone framework, meaning no reference to other frameworks would be necessary for SMEs to prepare financial statements that provide a true and fair view, the FRSSE would not achieve its goals (Laydon, 1997).

In contrast to this argument, a local study by Bugeja (2017) found that participants were in favour of GAPSME being in line with IFRSs and the previously developed GAPSE. This was said to give the national GAAP more credibility (Bugeja, 2017).

Stylianou (1997) found that partners in accounting firms claimed that true and fair view should be a principle that does not depend on the size of the firm and that emotions relating to the situation of owners of smaller firms should not be taken into consideration but logic and reason should prevail.

In the United Kingdom (UK), the FRSSE was initially opposed mostly by small practitioners which were already finding it difficult to adjust to the constant large changes in the profession at that time. The abbreviated accounts were deemed to not provide a true and fair view as they exclude vital information which would be needed for financial statements to be drawn up in line with such an important principle (PWC, 1999 as cited in Collis, 2012). Banks were also not satisfied with the limited information regarding financial performance that the shorter statements provided (Kitching et al., 2011 as cited in Collis, 2012). This bank dissatisfaction led to SMEs voluntarily still producing full audited financial statements in an attempt to improve their relationship with the bank and be in a better position to access external finance opportunities (Marriot et al., 2006).

The FRSSE was reportedly followed by 49% of firms in 2002 (ICAS, 2002 as cited in Reid and Smith, 2007). One of the primary reasons why accounting firms would not consider transferring to FRSSE was that the costs and time associated with the switch would simply outweigh the benefits (McAleese, 2001 as cited in Rossouw and Van Wyk, 2009).

2.5 – MAIN FACTORS CAUSING DIFFERENCES IN NATIONAL GAAPS

Financial reporting differs from one country to another, due to a number of factors considered in developing a national accounting framework as identified in previous literature.

The law and finance theory states that a common-law system is considered the most favourable basis for financial development and economic growth while civil-law systems are the least favourable (Graff, 2006). Graff (2006) found that although empirical findings are not as clear as the theory suggests, the idea that a legal system could have a significant impact on the development of corporate law in a particular country was supported. This therefore indicates that the legal system of a country must be considered when developing a local financial reporting framework or adopting an international one (Graff, 2006).

Economic growth is said to have an effect on the accounting system development of a country, as countries with higher economic growth rates tend to demand a more robust and sophisticated framework, which may lead them to adopting international frameworks such as IFRSs (Mehdbhi and Zeghal, 2006). A similar relationship was found with relation to the degree of economic openness of a country, with countries with a higher degree of economic openness more likely to adopt an international framework, this being highlighted as the most influential factor in such development decisions (Mehdbhi and Zeghal, 2006).

Education levels are another determining factor, as Mehdbhi and Zeghal (2006) found that countries with higher education levels are more likely to adopt an international accounting framework, such as those issued by the IASB.

The same study also concluded that a country having an Anglo-American culture and with a capital market already in place are also characteristics which increase the chance of international framework adoption.

Cultural membership in a group of countries is highly influenced by familiarity and language. These factors also have an effect on a country's inclination towards a

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particular accounting framework (Mehdbhi and Zeghal, 2006). This can be observed in the Anglo-American culture group, which due to the IASB being highly influenced by this culture and the language of communication being English, Anglo-American countries are more likely to opt for IFRSs than countries of another culture and language (Abdelsalem and Weetman, 2003 as cited in Mehdbhi and Zeghal, 2006).

Political influences are said to have an impact on the accounting framework adopted or developed by a country (Chua and Taylor, 2008). Orumwense (2015) states that in countries where the Ministry of Finance has complete or significant influence over the development of the accounting framework, such as in the Czech Republic and Nigeria, priority may be given to developing a framework that first and foremost meets the needs of the taxation department rather than improving the economic substance for other main users (Orumwense, 2015).

Such influences are clearer in ex-soviet states, in which a rule-based approach is considered to be more appropriate due to the conforming nature of the population of such countries, which is a direct repercussion of their totalitarian past (Bloom et al., 1998 as cited in Orumwense, 2015).

2.6 - DIFFERENCES IN FINANCIAL REPORTING FRAMEWORKS – LARGE DEVELOPED COUNTRIES

2.6.1 – United Kingdom

The FRSSE, issued in 1997, can be considered as a testament of successful differential reporting in practice (Koppeschaar, 2012). In fact, the FRSSE was used as a template by the IASB in developing the IFRS for SMEs framework and additionally by the MIA in developing the local GAPSME (Collis et al., 2017; Alexander and Micallef, 2011). Figure 2.2 illustrates the journey embarked on by the UK in its development of differential reporting.

Table 1. Key features of UK GAAP 1998–2016.

Publicly accountable entities	Non-publicly accountable entities			
From 1998	*Large*	*Medium*	*Small*	
Full, audited accounts guided by SSAPs, FRSs, UITFs	Full audited accounts guided by SSAPs, FRSs, UITFs	Abbreviated accounts for filing, but full audited accounts for shareholders guided by SSAPs, FRSs, UITFs	Abbreviated accounts for filing, but full audited accounts for shareholders guided by the FRSSE	
From 2005	*Large*	*Medium*	*Small*	
Full, audited accounts guided by EU-adopted IFRSs	Full audited accounts guided by SSAPs, FRSs, UITFs	Abbreviated audited accounts for filing, but full audited accounts for shareholders guided by SSAPs, FRSs, UITFs	Abbreviated, audit exempt accounts for filing, but full accounts for shareholders guided by the FRSSE	
From 2015	*Large*	*Medium*	*Small*	
Full, audited accounts guided by EU-adopted IFRSs	Full audited accounts guided by FRS 102	Abbreviated audited accounts for filing, but full audited accounts for shareholders guided by FRS 102	Abbreviated, audit exempt accounts for filing, but full accounts for shareholders guided by the FRSSE	
From 2016	*Large*	*Medium*	*Small*	*Micro*
Full audited accounts guided by EU-adopted IFRSs	Full audited accounts guided by FRS 102	Full audited accounts guided by FRS 102	Abridged, audit exempt accounts guided by FRS 102	Abridged, audit exempt accounts guided by FRS 105

Figure 2.2 – Summary of changes in the UK GAAP over the years. Source: Collis et al., 2017, pp. 238.

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Currently, from 2016 onwards, the UK has a three-tiered differential reporting system as illustrated visually in Figure 2.3.
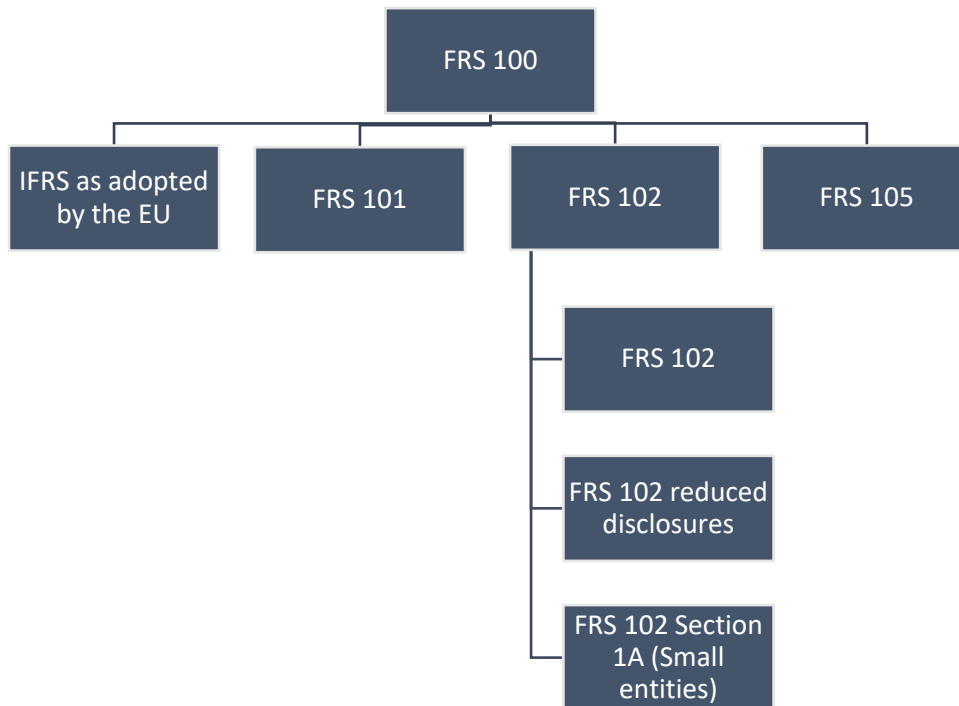
Figure 2.3 – The structure of financial reporting in the United Kingdom. Source: FRC, 2015 pp. 4.

- **FRS 100** (2012) determines which reporting framework is to be followed by specific entity types. PIEs are required to prepare accounts in accordance with IFRSs as adopted by the EU (Collis et al., 2017).
- **FRS 101** (2012) is a simplified framework for subsidiaries in a listed group to provide the same accounting required in the consolidated accounts but less disclosures in their individual financial statements. No recognition and measurement simplifications are allowed (Collis et al., 2017).
- **FRS 102** (2013) can be applied by both small and medium companies that are not PIEs. Section 1A then differentiates between the requirements of a small and medium company, with eligible small companies being required to produce a limited number of disclosures. Recognition and measurement requirements for Section 1A are the same as those set out in the rest of FRS 102 (FRC, 2015).

- **FRS 105** (2015) is the newly developed micro-entity regime framework transposed into UK law. It is primarily based on FRS 102 with significant presentation and recognition simplifications such as the abolishment of deferred tax recognition, the removal of related party disclosure requirements and all assets being measured at cost thus abolishing all fair value measurement requirements (FRC, 2015).

2.6.2 – United States of America (USA)

The United States is inclined towards the 'one size fits all' approach to financial reporting with the main arguments of proponents of such an approach being comparability, understandability and consistency (Mkasiwa, 2014).

Earlier studies found more support for the single GAAP approach, especially from lenders and creditors, however in recent years, concerns have been raised as to whether a blanket approach is a fair and equitable approach (Burns et al. 2012).

Knutson and Wichmann (1985) tested the '*equal importance assumption*' of disclosures in the USA. This study found that disclosures' importance varied with an entity's size and that as a bare minimum, disclosure requirements should be reduced for SMEs in the USA. This is an example of literature supporting differential reporting as early as 1985.

The American Institute of Certified Public Accountants (AICPA) recognised the severe reporting overload being suffered by American SMEs in 1995, as the sheer volume of standards issued by the FASB as at that time numbered a staggering 124 (Wright et al., 2012).

AICPA together with the FASB formed what is known as the Blue-Ribbon Panel in 2009 which put forward its recommendations to set up a separate board under the Financial Accounting Federation (FAF) entrusted with developing a differential reporting system in the USA and which would later be recognised as part of US GAAP. This proposal was however not accepted by the FAF (Wright et al., 2012).

Therefore, the USA makes for an interesting case of a large country, with clearly a high demand for a differential reporting system, which was held back by the powerful regulator (FAF) in charge of oversight, administration and financing of the standard setters.

2.6.3 – Canada

In great contrast with their American neighbours, Canada realised the benefits of differential reporting as early as 1980. It was concluded that the cost burden borne by SMEs in the preparation of their financial statements was one of the major problems such firms suffered from. Moreover, debates emphasised the over-complexity, lack of relevance and utility to financial statement users (Ashby, 1980 as cited in Koppeschaar, 2012).

A one-size-fits-all single set of GAAP without any size considerations was considered to be inadequate for SME stakeholders, suggesting private companies should not be required to comply with the same reporting requirements that listed companies are bound by (Feltham and Matthieu, 2000 as cited in Wright et al., 2012).

The Canadian Institute of Chartered Accountants (CICA) considered 2 possible approaches to implementing a differential reporting framework:

1) A 2 GAAP model consisting of Big GAAP and Little GAAP.
2) A single GAAP with particular standard exclusions applicable to private entities only.

The first option was discarded due to fear of confusion and possible discredit to the Canadian Profession as a whole, mainly attributed to the large differences that would arise between Big GAAP and Little GAAP (Wright et al., 2012).

The second option was adopted as it retained an element of standardisation and comparability between public and private companies, whilst eliminating particular aspects that were not relevant or useful to private companies and their users. This would therefore achieve the main goal of reducing the reporting and

consequentially the cost burdens borne by private companies (Feltham and Matthieu, 2000 as cited in Wright et al., 2012).

Noteworthy is the fact that the CICA recognised all private entities as eligible for using a simpler reporting framework, therefore using qualitative criteria rather than quantitative size thresholds to distinguish between large and small companies (Edwards, 2007).

2.6.4 – New Zealand

The '*Framework for Differential Reporting*' was issued by the Institute of Chartered Accountants of New Zealand (ICANZ) in 1994 with multiple revisions, the latest being in 2007 (Koppeschaar, 2012). This framework provides exemptions for SMEs including the exemptions from producing cash-flow statements, income tax accounting and segment reporting (Wright et al., 2012).

Therefore, similar to the UK, New Zealand developed a three-tiered differential reporting system where micro entities which qualify as exempt entities under the Financial Reporting Act of 1993 must abide by the minimal reporting requirements (Koppeschaar, 2012). Non-listed small and medium-sized entities are eligible for differential reporting if they are within the quantitative thresholds and there is no management-owner separation. The latter qualitative criteria highlights what is unique about New Zealand's system. All large companies and PIEs are not eligible for differential reporting and must abide by all the accounting standards.

The detailed categorisation of entities through quantitative and qualitative criteria makes this differential reporting system one of the most comprehensive world-wide (Baskerville and Simpkins, 1997:14 as cited in Koppeschaar, 2012).

2.7 - DIFFERENCES IN FINANCIAL REPORTING FRAMEWORKS - SMALL AND DEVELOPING COUNTRIES

2.7.1 – Romania

The fall of communism in 1989 was the catalyst to the embarkment of the Romanian profession in developing an accounting system which was suitable for its market specification (Ionaşcu et al., 2007 as cited in Bunea et al., 2012). Figure 2.4 illustrates a timeline of the development stages that the Romanian accounting system evolved through.

1990 - 1998	1999 - 2005	2006 - to date
• Creation of the Accounting System	• Harmonisation with EU Directives and IASs	• Compliance with EU Directives and IFRSs

Figure 2.4 - Timeline illustrating the main development phases of the Romanian financial reporting system over the years. Source: Bunea et al., 2012, pp.31.

Through cooperation with French Institutions, the new Romanian GAAP was developed and tested in 1993. In 1994, Romanian GAAP was issued for use in practice (Deac, 2013).

Differential reporting was integrated in the simplified system as per the Government Decision no. 704/1993, which allows SMEs to use a simplified framework. SMEs could opt to use this framework provided that the necessary criteria are met in two consecutive years. The difference between the two frameworks was purely relating to disclosure requirements (Bunea et al., 2012).

In 2002, the simplified accounting framework was also harmonised with EU and IAS regulation. SMEs could prepare a balance sheet, profit and loss account and explanatory notes, while micro entities were not required to provide notes at all (Bunea et al., 2012). At present, SMEs eligible through the size criteria produce an abridged balance sheet, abridged profit and loss account and explanatory notes. The production of statements of changes in equity and cash flow statements are left optional. SMEs are also not bound by a statutory audit requirement (Bunea et al., 2012).

Bunea et al. (2012) found that 52.6% of expert accountants questioned were of the opinion that the simplifications are not yet at a reasonable level. Quantitative thresholds in place were still deemed better than a qualitative alternative, but changes to such thresholds were considered necessary.

2.7.2 – Swaziland

In Swaziland, SMEs are determined through quantitative thresholds relating to asset value, annual turnover and staff population (Muyako Sithole, 2015). All listed entities and PIEs must prepare their financial statements in accordance with full IFRSs, while qualifying SMEs are not legally required to publish financial statements by the CA of 2009 (Muyako Sithole, 2015).

Differential reporting in Swaziland is therefore optional and not legally imposed. If SMEs voluntarily still opt to produce financial statements, they may follow full IFRSs or IFRS for SMEs. The latter is an option introduced by the Swaziland Institute of Accountants (SIA) allowing compliance with IFRS for SMEs in 2010 (IFAC, 2016).

Muyako Sithole (2015), found that all SME questionnaire participants, which spanned across several industries, explained that the reporting framework used before IFRS for SMEs, being IFRSs or other frameworks, were adequate. On the other-hand 23.53% of stakeholders interested in SME financial information claimed that these frameworks did not meet their needs (Muyako Sithole, 2015).

2.7.3 – Nigeria

The Financial Reporting Council of Nigeria (FRCN) announced that a transition to adopt IFRS for SMEs was to commence on January 1st, 2012 (Ezeagba, 2017). This culminated in all qualifying SMEs in Nigeria being required to produce their financial statements according to IFRS for SMEs by January 1st, 2014.

The success of the implementation of such a framework mainly lies in the accountants' hands, as SMEs still require the necessary awareness and knowledge of the benefits and usefulness of such a framework (Mukoro and Ojeke, 2011 as cited in Ezeagba, 2017).

Ezeagba (2017) finds that the following factors contribute to the inadequacy of financial records produced by such entities:

- Poor credit facilities granted to SMEs leading to lack of resources
- SMEs not following the National Action Plan for IFRS implementation in Nigeria, highlighting the lack of enforcement of Accounting regulation
- Lack of manpower necessary to properly comply with all requirements

Some recommendations to improve this situation include:

- Free professional services provided to SMEs by professional bodies
- Commercial bank units which aid SMEs in providing documentation necessary for easy access to financing
- Increases in credit lines granted to SMEs by banks (Ezeagba, 2017).

2.8 - IFRS FOR SMEs AS AN INTERNATIONAL DIFFERENTIAL REPORTING FRAMEWORK - PROS AND CONS

IFRS for SMEs was issued for use by the IASB in July 2009 (Kaya and Koch, 2015). This framework targets all non-PIEs. Other qualitative or quantitative criteria which have to be met for a company to qualify as an SME have been entrusted to national regulators (Van Wyk and Rossouw, 2009). Table 2.1 highlights the major differences between full IFRS and IFRS for SMEs:

Full IFRSs	IFRS for SMEs
Standards numbered as they are published	Organised by topics, following an order similar to the UK's FRSSE
Almost 3000 pages	Under 300 pages
Around 3000 disclosure points	About 300 disclosure points
Updated almost monthly	Updated once every two to three years

Table 2.1 – Main differences between Full IFRSs and IFRS for SMEs. Source: Pacter, 2009, pp.9.

Kaya & Koch (2015) stated that at that time, over 70 countries had already applied or were planning to apply IFRS for SMEs. They concluded that countries with the following characteristics are more likely to adopt IFRS for SMEs:

- Previous IFRS background
- Inability to develop a national GAAP, such as Barbados (ICAB, 2007 as cited in Kaya and Koch, 2015)
- Lower quality governance institutions

2.8.1 - European Views on IFRS For SMEs

The European Commission (EC) called for the opinion of EU stakeholders on the framework, to which it received in excess of 200 responses spanning across 26 member states (EC, 2010). The suitability of IFRS for SMEs in Europe was agreed upon by the majority of member states. Proponents of IFRS for SMEs

argued that the following were considered to be the main advantages of such a framework:

- Increased harmonisation and comparability
- Facilitation of cross-border trade and international growth of SMEs
- Higher attraction to foreign investors reducing the cost of capital for SMEs
- Preparation of consolidated accounts for multinational groups would be simpler and less costly
- Easier to follow than IFRSs as adopted by the EU (EC, 2010).

The majority of member states seemed to suggest that IFRS for SMEs should be applied in the EU. A common opinion was that implementation should be done in line with EU directives and be limited to member state options not obligations (EC, 2010).

IFRS for SMEs was however also met with criticism and scrutiny. In the same European consultation (EC, 2010), opponents of IFRS for SMEs argued that such a framework:

- Is still too complex for SMEs, specifically the smallest ones
- Will increase the administrative burden and costs of preparing individual SME accounts
- Leads to a competitive disadvantage for SMEs due to extensive disclosure requirements when compared to other simplified national GAAPs
- Focuses on international comparability which is not relevant to locally operating SMEs
- Is still not suitable for internal management of SMEs
- Targets share capital providers and does not address the specific needs of SME financial information users
- Makes use of a top-down approach, whilst a bottom-up approach (such as that used in EU Directives) is considered to be more appropriate. For example, full IFRSs do not allow Last-in-first-out (LIFO) and given that the principles of IFRS for SMEs have to follow IFRSs, LIFO will also not be allowed. This will therefore not change anything for SMEs, which is not considered to be the optimal situation (Pacter, 2009; EC, 2010).

2.8.2 - Country Specific Study – Germany

In Germany, field tests were conducted on local SMEs by the Accounting Standards Committee of Germany (ASCG) in May 2007, to gather opinions about IFRS for SMEs (ASCG, 2008). Results show very similar advantages and disadvantages to the ones listed above. Certain concerns raised by preparers did however stand out, including:

- Burdensome and cost intensive notes were still required.
- Numerous standards lacked clarity and understandability, specifically those relating to financial assets and liabilities and income taxes (ASCG, 2008).

Germany was also considered to suffer additional costs upon converting from German GAAP to IFRS for SMEs due to the inherent differences between the frameworks (ASCG, 2008).

2.8.3 - Country Specific Study – Romania

Costs associated with shifting from one framework to another is also mentioned as an unwelcome indirect cost in a Romanian Study (Bunea et al., 2012). This same study also includes translation and professional training costs as problems arising during the implementation of IFRS for SMEs in Romania. Taking this into consideration, the study concludes that Romanian stakeholders did not consider IFRS for SMEs adequate to improve accounting in Romania. IFRS for SMEs was opposed by Romanian preparers due to their unfamiliarity with IFRSs as these were only used by publicly traded companies (Bunea et al., 2012).

2.8.4 - Country Specific Study – South Africa

Koppeschaar (2012) analysed the perception of IFRS for SMEs in South Africa. The overall perception of IFRS for SMEs by 60% of preparers was that it does not reduce the reporting burden for SMEs substantially. Some main recommendations which over 90% of respondents agreed upon included:

- Further simplification of measurement requirements;
- Even less disclosure requirements; and
- Reduction in standards applicable to SMEs (Koppeschaar, 2012).

Two direct respondent quotes highlight the gravity of the situation:

> "Special standard for SMEs – this standard (IFRS for SMEs) is not simple… Special standards must be meaningful – not like IFRS for SMEs, which is no help at all."
>
> (Koppeschaar, 2012, pp.64)

2.8.5 – Country Specific Study - Swaziland

Muyako Sithole (2015) found that in Swaziland, knowledge of the IFRS for SMEs framework was a clear problem, as 77.08% of respondents expressed that they were not aware of the standard to begin with. The main challenges listed by respondents based on the financial framework at that time included:

- Lack of proper documentation and financial expertise;
- Lack of financial and resources in general;
- Lack of up to date information of IASs; and
- An overload of disclosures which were not understandable (Muyako Sithole, 2015).

Although most stated that they were not knowledgeable on IFRS for SMEs, they expressed their expected benefits from implementing the framework. Some of the benefits mentioned include:

- Increases in simplification and understandability,
- More uniformity and transparency across all industries (Muyako Sithole, 2015).

The main costs associated with the adoption of IFRS for SMEs mentioned by respondents in Muyako Sithole's (2015) study include:

- Higher costs due to the need for more resources;
- More expertise required; and
- Higher professional and training costs, especially during the early transition period.

2.9 – MAIN USERS OF SME FINANCIAL STATEMENTS

Many studies have tried to prove the fact that SME users are different from larger company users and therefore challenging the IASB Conceptual Framework which states that the main users of financial statements are existing and potential investors, lenders and other creditors (IASB, 2015). Similar users were identified in a discussion paper published by the Financial Reporting Council (FRC) and the Department for Business Innovation and skills (BIS) in August 2011, which further elaborated that customers and government agencies were the main reliant users of micro company financial information (BIS, 2011).

2.9.1 – Owner-Managers

Owner managers had varied opinions regarding the usefulness of the end of year financial statements prepared according to Canadian GAAP. Many stated that such statements were not helpful in running their business whilst also expressing their concerns that financial information produced in GAAP financial statements

was redundant to them and external users (AcSB, 2005). On the other hand, others considered them to be a good year-end recap and served as a structure for internal statements (AcSB, 2005).

A UK study found that only 41% of directors taking part considered annual reports as a contribution to management information (Page, 1984 as cited in IFAC, 2006). Another UK study's respondents suggested other financial information such as cash, liquidity and cost levels were used by owner managers, together with non-financial indicators such as the debtor collection period (Jarvis et al., 2000 as cited in IFAC, 2006).

As most local studies suggest that SMEs prepare financial statements purely because they are legally obliged to do so, an owner manager suggested that the calculation of ratios from these statements is the only benefit that can be derived for internal use (Borg et al., 2015).

In his dissertation, Borg (2009) found that owner managers were more interested in management accounts, which were prepared in simpler and more understandable manner for owners (Borg, 2009).

In their presentation, Borg et al. (2015) looked at specific elements in financial statements and how important each is to owner-managers.

- SOCFs were not considered useful for decision making due to their complexity, but cash flow information is considered vital and is mainly extrapolated through management accounts.
- Disclosures were not considered clear and understandable, this being the reason why most owner-managers stated that they mostly ignore the notes altogether.
- Fair value measurement was not considered to be relevant to SME owner-managers as such firms have little to no fixed assets and tend to not invest in financial instruments (Borg et al., 2015).

2.9.2 - Banks and Institutions

Banks were singled out as the main external users of SME financial information (Schiebel, 2006). Owners were also considered the main internal users with individual purposes such as determining an adequate amount of remuneration rewards (Sian & Roberts, 2006). In Canada, the Accounting Standards Board (AcSB) identified lenders such as banks as the main external users of SME financial statements (AcSB, 2008).

In Malta, financial statements were considered important for banks to assess applications for funds or their current debtors. However, due to the lack of information found in GAPSME financial statements and annual accounts being considered untimely, they would never fully rely on such information (Casha, 2013). Therefore, qualitative measures were also considered useful such as customer profiling and trend analysis (Mallia, 2014).

2.9.3 - Tax Authorities

In a study questioning professional accountants, carried out in Romania, the tax authorities were identified as the main user, followed by lenders (Bunea et al., 2012). In a similar local study, the main external users in Malta were identified as banks, other lenders and creditors, the Inland Revenue Department and the regulator (Mizzi, 2009).

The comment letter sent by the MIA to the IASB in response to the Discussion Paper - Preliminary views on Accounting Standards for Small and Medium-sized Entities states that investors, lenders and government agencies were considered the main users of SME financial statements while suppliers and trade creditors were mentioned as other external users (MIA, 2004).

2.10 – DIFFERENTIAL REPORTING IN MALTA

2.10.1 – GAPSE

GAPSE was developed in line with the UK's FRSSE and elements of IFRS, however with the local scenario always given priority (Zammit, 2011). Both quantitative and qualitative criteria were used to distinguish which firms were eligible to make use of GAPSE (Zammit, 2011).

GAPSE included reductions in disclosures as well as simplified recognition and measurement methods. It is estimated that disclosures required under GAPSE numbered to 300, which is a reduction of approximately 90% when compared to the 3000 required under IFRSs (Deloitte, 2009). On the other hand, measurement and recognition simplifications were aimed to target the areas where SMEs would appreciate them the most, such as:

- Property, plant and equipment
- Intangible assets
- Investments in subsidiaries and associates
- Financial assets (Dingli, 2009 as cited in Zammit, 2011)

Some main advantages of the GAPSE framework included the fact that it was drawn up in consistency with the 4th and 7th EU Directives, which provided stability and credibility (Dingli, 2009 as cited in Zammit, 2011). Caruana (2009) found that all eighteen auditor respondents, varying in size, suggested GAPSE was better than IFRS for SMEs as it took into consideration the specific needs of Maltese SMEs whilst also reducing the intensity of testing which was required for an audit of these SMEs (Caruana, 2009).

However, GAPSE was hardly considered the perfect framework, which can be clearly seen with the low take-up rate of 33% by 2013 (Times of Malta, 2013). Some flaws which were said to have contributed to this were:

- Banks and other stakeholders still required full audited accounts
- Lack of awareness of the framework in general
- Further areas of simplification needed such as omitting the SOCF requirement
- The requirement to account for deferred taxation
- Thresholds not focussing on the firms that suffer the most (Times of Malta, 2013; Zammit, 2011)

These issues together with the introduction of the SAD, provided motivation to re-think the national SME framework, and therefore GAPSME was developed in order to improve on GAPSE and to transpose the new directive into Maltese law.

2.10.2 – GAPSME

GAPSME brought along some major changes with regards to SME financial reporting in Malta. The scope of GAPSME is broader when compared to that of GAPSE, both in terms of quantitative and qualitative criteria (Dimech, 2016).

Dimech (2016) carried out a preliminary feedback exercise of GAPSME expectations. Interestingly, it was found that owners, which were the main targets of many simplifications, did not perceive major differences with the issuance of GAPSME. This suggests that the main goal of the framework would not be achieved (Dimech, 2016).

Other stakeholders, such as banks, argued that the simplifications were too much, and that the financial statements are not providing enough information. Bank respondents highlighted the absence of the SOCF, which was said to provide vital cash related information to credit institutions, while a Malta Association of Credit Management (MACM) interviewee clearly stated that in his opinion, GAPSME would be a step backwards for financial information in Malta (Dimech, 2016).

The profession members which were part of this study did not perceive GAPSME to be beneficial to them, mentioning the following main concerns:

- Confusion and a higher workload in the early years;
- Reduction in the use of IFRSs which may result in a loss of knowledge and relevance of the international standards, undesirable for the national profession;
- Reduction in the financial institution strength of Malta when compared to those of other EU members;
- Fear of the development of a two-tiered profession; and
- Anticipated reduction in fees due to clients demanding lower charges for the reduced amount of audit work required (Dimech, 2016).

2.11 – CONCLUSION

This study will aim to build on the above literature, with special reference to the take-up of GAPSME a few years after its issuance and the opinions of SMEs and auditors regarding the differential reporting framework developed and issued in Malta.

Chapter 3

Research Methodology

3.1 – INTRODUCTION

This chapter provides an insight into the methods which were employed throughout the study in order to satisfy the research objectives. Research took place over a seven-month period between October 2018 and April 2019.

3.1 - INTRODUCTION

3.2 - RESEARCH OBJECTIVE DEVELOPMENT

3.3 - MIXED RESEARCH METHODOLOGY
- •3.3.1 - Reasons for Adopting a Mixed Methodology
- •3.3.2 - Explanatory Sequential Mixed Methods Design

3.4 - QUANTITATIVE DATA
- •3.4.1 - Population and Sample of Study
- •3.4.2 - Quantitative Data Collection
- •3.4.3 - Preliminary Assessment of Quantitative Data
- •3.4.4 - Binary Logistic Regression

3.5 - QUALITATIVE DATA
- •3.5.1 - Semi-Structured Interviews
- •3.5.2 - Sample Size and Participant Selection
- •3.5.3 - Transmission of Interviews
- •3.5.4 - Qualitative Data Analysis

3.6 - LIMITATIONS OF THE STUDY
- •3.6.1 - Quantitative Data Limitations
- •3.6.2 - Qualitative Data Limitations

3.7 - CONCLUSION

Figure 3.1 – Chapter 3 Overview.

3.2 – RESEARCH OBJECTIVE DEVELOPMENT

Through the review of literature, which was the basis for the in-depth literature review in chapter 2, differential reporting was identified as one of the predominant topics featured in accountancy studies and international accounting news. Taking into consideration the importance of the debates surrounding differential reporting and the recent world-wide movement towards it, combined with the relatively recent issuance of a new differential reporting framework (GAPSME) in Malta, a study of this nature was considered useful, relevant and timely in nature.

Preliminary conversations were also carried out with academics and professionals which are knowledgeable in the application of differential reporting in Malta, all of whom supported the study's objectives and confirmed its relevance to the Maltese accountancy profession.

The aim of this dissertation was therefore to give a comprehensive outlook on the implementation of the GAPSME framework in Malta while understanding factors which may influence the Maltese SMEs' framework choice. Such a study also had another purpose, which was to voice the opinions, concerns and suggestions of owners and auditors of SMEs, thus serving as a feedback exercise of GAPSME simultaneously.

3.3 – MIXED RESEARCH METHODOLOGY

3.3.1. – Reasons for Adopting a Mixed Methodology

A mixed method approach was identified as the most comprehensive manner by which the necessary data could be collected (Creswell, 2014). This decision was taken after analysing the literature in support and against all 3 main data collection methods, which are namely:

- Quantitative research
- Qualitative research
- Mixed methodological research.

Past dissertations having similar objectives to this study were also considered, where the methodology section provided information relating to the approach taken and any limitations which they encountered in using their selected research methods.

Using a combination of both quantitative (Sec. 3.4) and qualitative (Sec. 3.5) methods is said to enhance a study's validity as the strengths of one method will counteract the deficiencies of the other (Yeasmin and Rahman, 2012). Quantitative research is considered the best and most efficient way to collect, evaluate and categorise large volumes of data. (Choy, 2014) This does however hinder its ability to understand behaviour or relationships when used in an isolated manner (Tewksbury, 2009).

This is balanced out by the nature of qualitative research which allows a more in-depth investigation into understanding the data, thoughts and opinions of participants (Tewksbury, 2009; Hancock, 1998). This does however mean that much smaller sample sizes are used in the latter due to the nature by which such data must be collected (Dieronitou, 2014).

3.3.2 - Explanatory Sequential Mixed Methods Design

For the purposes of this study, the explanatory sequential mixed methods design was used. In this method, the quantitative data is collected and analysed as the first part of a two-phase project design (Creswell, 2014). The quantitative data is then used to provide a better basis on which the second phase, being the qualitative phase can be carried out (Creswell, 2014).

The main aim behind this sequential structure is that the qualitative data helps interpret the quantitative data while the quantitative data allows a more focussed and structured approach going into the qualitative phase of the project (Creswell, 2014). Figure 3.2 illustrates the process used in this dissertation in a simpler manner.
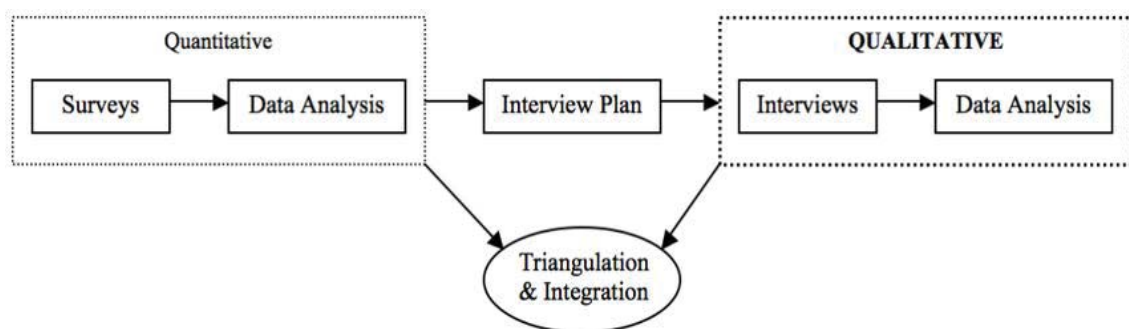
Figure 3.2 - Process of the explanatory sequential mixed methods design. Source: Philip Fei Wu, 2011, pp.11.

Linking specifically the above to the chronological order in which this study was carried out:

1) Collection of data from financial statement analysis using Microsoft Office Excel.
2) Excel spreadsheets imported into IBM SPSS Software Version 26 for further analysis.
3) Binary logistic model together with statistical testing used to identify data relationships.
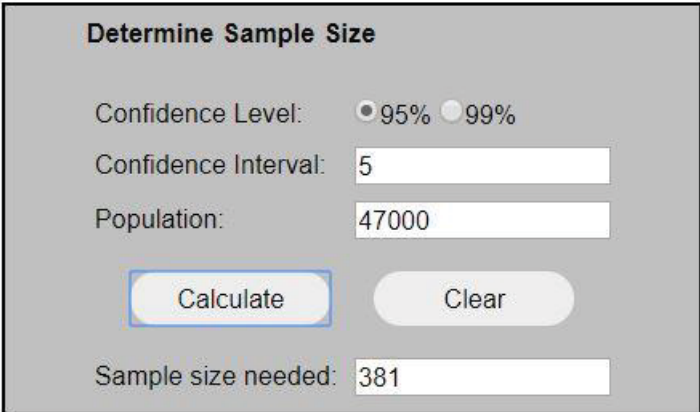
4) Results of quantitative data used in forming the semi-structured interview schedules.

5) The interviews were carried out and transcripts written-up.

6) The results from the statistical model outputs and the interview replies were compared and integrated together to form the finalised results and allow a holistic interpretation of the study and its findings.

3.4 – QUANTITATIVE DATA

3.4.1 – Population and Sample of Study

The initial population of this study includes all companies which were registered in Malta as at May 2018. This population was then limited to companies which were incorporated before 2012, leaving a valid population of 47000 companies which was used in this study. The official list of registered companies as of May 2018 was obtained through a Malta Financial Services Authority (MFSA) director.

A sample size of 381 was determined through an online sample size calculator at a confidence level of 95%, implying a maximum margin of error of 5%. Figure 3.3 shows the original output of this calculation.

Figure 3.3 - Output of online sample size calculation.
Source: https://www.surveysystem.com/sscalc.htm

In order to confirm the above sample size, the sample size was also calculated through the power equation. A step-by-step illustration of this can be found in A3.1. Although a sample size of 381 would provide a margin of error of 5%, data for 399 companies was obtained in order to allow for any outliers or unreliable data entries.

3.4.2 – Quantitative Data Collection

The collection of the quantitative data consisted of financial statement analysis of 399 randomly sampled firms through the ROC Database. This exercise was carried out over 2 weeks in the beginning of March.

Google's random number generator was used to produce a number between 1 and 47000. This would correspond to the Company ID, which is a unique reference code given to each company registered in Malta, and results in that company being selected.

A comprehensive list together with an explanation of all data fields which were collected for each company can be found in A3.3.

3.4.3 – Preliminary Assessment of Quantitative Data

IBM SPSS Version 26 was used as an analytical statistical tool on data collected.

Descriptive statistics were generated in order to better understand the demographics of the data gathered through the companies' financial statements (A4.1).

All continuous variables were found to violate the normality assumption through the Shapiro-Wilk test, the results of which can be found in A3.2. Therefore, to enable more in-depth analysis of the quantitative data, several non-parametric tests were carried out, the results of which are discussed in the next chapter.

A detailed explanation of the following non-parametric tests used is included in A3.5.

- Spearman's Correlation Test
- Chi-Square Test of Independence
- Mann-Whitney U Test

Multivariate analysis, including the Spearman's Correlation test for continuous variables and Chi-Square tests for categorical variables, were used to identify and analyse relationships between the dependent and independent variables on a stand-alone basis. This allowed the researcher to identify variables which should be excluded from the model due to high correlations between themselves and the dependent variable.

The Eligibility to use GAPSME variable was excluded due to its high correlation with the dependent variable (Use of GAPSME). This can be observed through the cross-tabulation (Table A3.5), where 100% of firms which use GAPSME were found to be eligible to use GAPSME. The Chi-Square test of independence carried out between these two variables was statistically significant at the 0.005 level of significance, which indicates a relationship between the two variables. In order to gauge the strength of this association, the Cramer's V value of 0.293 was referred to, which indicates a moderately strong association, thus warranting the independent variable's exclusion. Result tables of the above tests can be found in A3.6.

Significant correlations were also observed through a Spearman's Correlation test between all the continuous variables.

Correlations found significant at the 0.01 level were observed between the following (Table A3.8):

- Debt/Equity ratio in 2016 and Debt/Equity ratio in 2015
- Current ratio in 2016 and Current ratio in 2015
- Government Grants/ Tax Credits in 2016 and Government Grants/Tax Credits in 2015/2014
- Proportion of Revalued Assets and Government Grants/ Tax Credits in 2016

The above resulted in the elimination of the following variables from the model:

- Debt/Equity ratio in 2015
- Current ratio in 2015
- Government Grants/Tax Credits in 2015/2014
- Proportion of Revalued Assets

3.4.4 – Binary Logistic Regression

Given that the dependent variable is a binary decision of 'Yes' in the case of GAPSME adoption and 'No' in the case of GAPSME non-adoption, a binary logistic regression model was selected. A detailed explanation of the binary logistic regression model can be found in Section A3.4.

A Logistic regression is a generalized linear model mainly used to investigate and identify how independent variables are related to the probability of obtaining a particular outcome in the dependent variable. This type of regression can also be used to establish the probability of an event occurring, given the explanatory variable values. In addition to this, a logistic regression model also estimates the odds ratio for each combination of values of the explanatory variables in the final parsimonious model (Tabachnick et al., 2007 as cited in Montebello, 2010).

3.5 – QUALITATIVE DATA

3.5.1 – Semi-Structured Interviews

In-depth semi-structured interviews were conducted in order to substantiate and provide further insight into the conclusions which could be drawn from this dissertation's results. The interviews consisted of open-ended questions in order to try and gain a better understanding of the reasoning behind the choice of whether GAPSME was considered beneficial or not (Refer to A6 and A7).

3.5.2 – Sample Size and Participant Selection

A total of 8 interviews were carried out, which were split between two sample populations comprising of auditors and SME representatives.

The sample of interviewees was further categorised as follows:

- Big 4 Audit Firms (2)
- Mid-tier Audit Firm (1)
- Small/Medium Practitioner (1)
- Sole Practitioner (1)
- GAPSME Adopters (3)

When determining the number of interviews which were to be conducted, the above categorisation and number of interviews was considered appropriate, especially considering the purpose of these interviews was to compliment the findings obtained through the quantitative data and provide an insight into possible reasons behind relationships established through the statistical model results.

Other dissertations, such as Zammit (2011), were also considered in establishing the appropriate sample size, where the pattern observed was that interviews with

SME owners or members of management were often turned down due to perceived lack of financial knowledge to answer the questions. This is also why 5 auditor interviewees were approached compared to 3 SME respondents, as the auditors' professional opinion and vast experience in dealing with SMEs in their client portfolio is expected to provide answers which are more relevant to this study's objectives.

The interviews with SMEs were carried out with the key person in the company's finance department, and where the accounting function was totally outsourced, the person within the outsourced company which handles the accounts function of that particular SME was interviewed. The interviews with auditors were carried out with the person who had first-hand experience in auditing SME financial statements over a number of years.

3.5.3 - Transmission of Interviews

All interviewees were contacted through emails containing a general explanation of the study and the formal letter of invitation (A8 – A10). Most respondents were then contacted through telephone to set up an appointment for the interview to take place.

Due to ethical considerations, before the interview ensued, all interviewees were briefed on how the interview would be carried out, the purpose behind the interview and once again ensured of the anonymity of their responses in order to encourage more detailed answers. The Information sheet together with the Consent form were also provided at this point.

The interviews were voice recorded, with the interviewees' consent, in order to enable the compilation of a more accurate transcript. This is vital in achieving the necessary discussion which would put the interviewee at ease and allow the thorough explanation of reasoning which was the purpose of this qualitative exercise.

3.5.4 – Qualitative Data Analysis

The analysis of qualitative data was mainly done through producing transcripts of the interview discussion and categorising responses of specific respondents through thematic analysis. This made it possible for the broad answers to be easily sorted into response categories, enabling more structured findings to be deduced and analysed (Dimech, 2016).

After all interview responses were categorised, comparison of response categories ensued, in an attempt to establish particular patterns which would explain partially or indicate the representative views of one category of firms with respect to another.
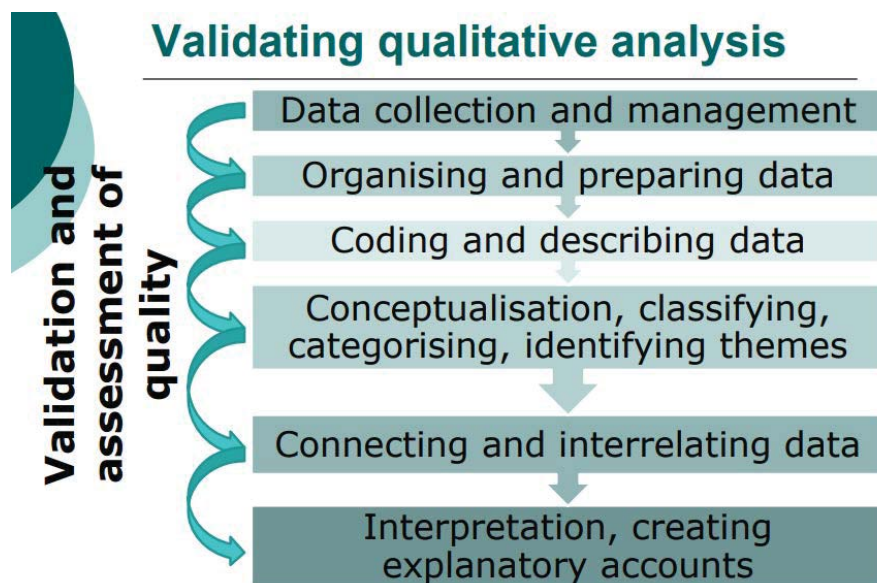
Figure 3.4 - Process of quality assessment followed in qualitative data analysis. Source: Barnes and Hoyos, 2012, Slide 29.

Figure 3.4 illustrates the basic step-by-step process that was followed in order to ensure that the quality of the assessment of the interview responses was preserved.

3.6 – LIMITATIONS OF THE STUDY

3.6.1– Quantitative Data Limitations

- Companies which were incorporated after 2012 were excluded from the sample. This was due to the fact that a number of independent variables required an analysis over a period of time. This may make the data less representative of the entire Maltese SME population, also due to the presence of dissolved companies which are still included in this study's broad population.

- Due to the exemption for small private exempt companies under the proviso in Section 183(2) of the CA. (Cap.386 of the Laws of Malta), which allows such companies the option to not file the Income Statement (IS) with the ROC, independent variables in relation to figures shown in the IS could not be used.

- Logistic regression models have their own limitations which include lack of robustness, bias in the value of parameters estimates, problems with rare events such as the dataset containing much less No (zeros) than Yes (ones) for some variables and problems related to sampling design (Tabachnick et al., 2007 as cited in Montebello, 2010).

3.6.2– Qualitative Data Limitations

- The main limitation found in carrying out interviews with SME representatives was the lack of in-depth answers which was partially counteracted through probing and further clarification of questions.

3.7 – CONCLUSION

This chapter gave a detailed description of how this study was carried out, including the reasoning behind the selected methods for data collection and data analysis.

Chapter 4

Findings and Discussion

4.1 – CHAPTER INTRODUCTION

This Chapter will illustrate the findings that have been generated throughout this study, together with a discussion of such findings in which an interpretation and comparison with expected results will be carried out. The chapter has been divided into three main sub-sections, each corresponding to one of the three research objectives stated in Chapter 1.

A clear distinction is made between the findings, which represent the actual output of statistical models and interviews carried out, and the discussion of such findings which will include the author's interpretation of such findings and comparison with relevant literature. The two sections will be clearly distinguishable through subheadings for each sub-section.

4.1 - INTRODUCTION

4.2 - RESEARCH OBJECTIVE 1 - GAPSME IMPLEMENTATION LEVEL IN MALTA

- 4.2.1 - GAPSME Take-up - Findings
- 4.2.2 - GAPSE Take-up - Findings
- 4.2.3 - Reasons Why GAPSME Has a Higher Take-up than GAPSE - Findings
- 4.2.4 - Discussion of Findings

4.3 - RESEARCH OBJECTIVE 2 - COMPANY SPECIFIC FACTORS IMPACTING FRAMEWORK CHOICE

- 4.3.1 - Descriptive Analysis
- 4.3.2 - Binary Logistic Regression - Findings
- 4.3.3 - Discussion of Findings

4.4 - RESEARCH OBJECTIVE 3 - GAPSME FEEDBACK BY AUDITORS AND SME REPRESENTATIVES

- 4.4.1 - Pragmatic Benefits of GAPSME - Findings
- 4.4.2 - Concerns Relating to GAPSME's Perceived Inferiority - Findings
- 4.4.3 - The Costs of GAPSME Adoption - Findings
- 4.4.4 - Who Influences the Financial Reporting Decision - Findings
- 4.4.5 - The Main Drawbacks of GAPSME - Findings
- 4.4.6 - Discussion of Findings

4.5 - CONCLUSION

Figure 4.1 - Chapter 4 Overview.

4.2 – RESEARCH OBJECTIVE 1: GAPSME IMPLEMENTATION LEVEL IN MALTA

The take-up rate of a framework is a good indicator of how successful it has been implemented and how adequate and useful it is deemed to be by its users. This section will therefore look at the GAPSME take-up during its first year of applicability. This can be compared to the take-up rate of GAPSE as at 2015 to further understand whether GAPSME is more widely used compared to its predecessor.

4.2.1 – GAPSME Take-Up – Findings

From the sample of 399 companies analysed in this study, 5 companies did not meet the GAPSME quantitative thresholds while another 3 entities qualified as PIEs. Therefore, the companies which were eligible to use GAPSME numbered 391 and represent 98% of the sample. As 99.8% of Maltese companies are SMEs, an eligibility level close to 100% was expected and suggests that the sample selected can be considered representative of the population (SBA Fact Sheet, 2018).

Out of these 391 eligible entities, 322 prepared their 2016 financial statements according to GAPSME, indicating a percentage take-up rate of 82.4%, which is illustrated in figure 4.2.
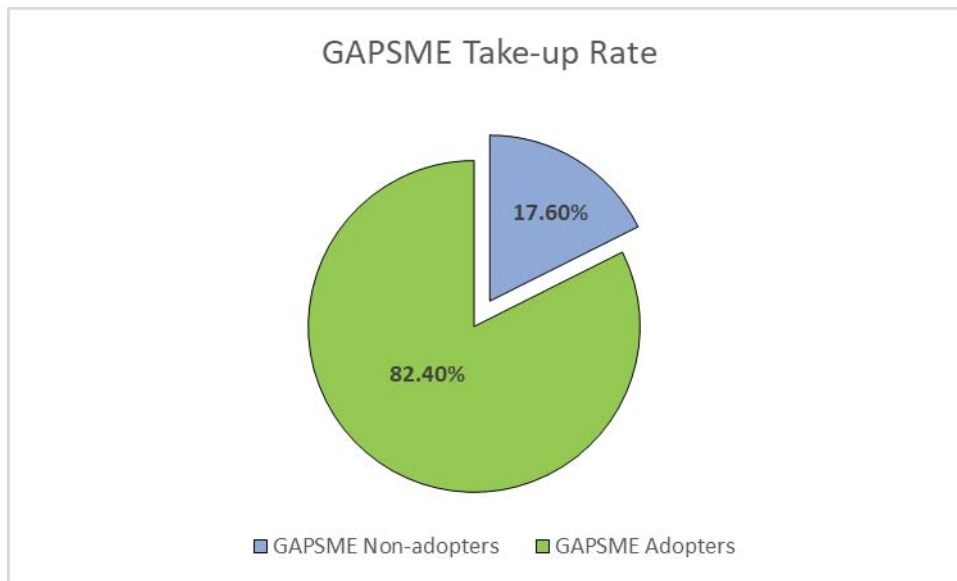
Figure 4.2 - Pie-chart illustrating the GAPSME take-up

This intrinsically suggests that there was a sizeable proportion of firms (69/391) that were eligible to use GAPSME but opted to still prepare their financial statements in accordance with IFRSs as adopted by the EU. Whilst all auditor interviewees suggested that it was rare that an eligible SME does not opt to prepare GAPSME financial statements, a number of situations were mentioned where eligible SMEs often are obliged to prepare their financial statements according to IFRSs as adopted by the EU. Such situations are listed below.

Some SMEs which are subsidiaries of a foreign parent company are often restricted by such parent to prepare their financial statements in accordance to the more comparable IFRSs as adopted by the EU.

SMEs which have obtained finance through a foreign bank could be obliged to prepare IFRS financial statements through a restrictive clause in the relevant loan covenants. As stated by an interviewee:

> "If you have foreign banks, where in their loan covenants they stipulate that they require IFRS financial statements, even if they would want to produce financial statements under GAPSME, because of these external restrictions they would not be able to opt for it."

(Auditor interviewee 1)

Therefore, from the situations mentioned above, auditor respondents clearly suggest that SMEs eligible to use GAPSME very rarely reject GAPSME through a voluntary decision, but do so due to external restrictions imposed upon them.

4.2.2 – GAPSE Take-Up – Findings

As historical data through financial statement analysis from 2016 to 2012 was collected, it was also possible to compare the take-up of GAPSME in its first year of use (2016) to the take-up of GAPSE in its last year of use (2015). As seen in figure 4.3, the take-up of GAPSE in 2015 was 49.87%.
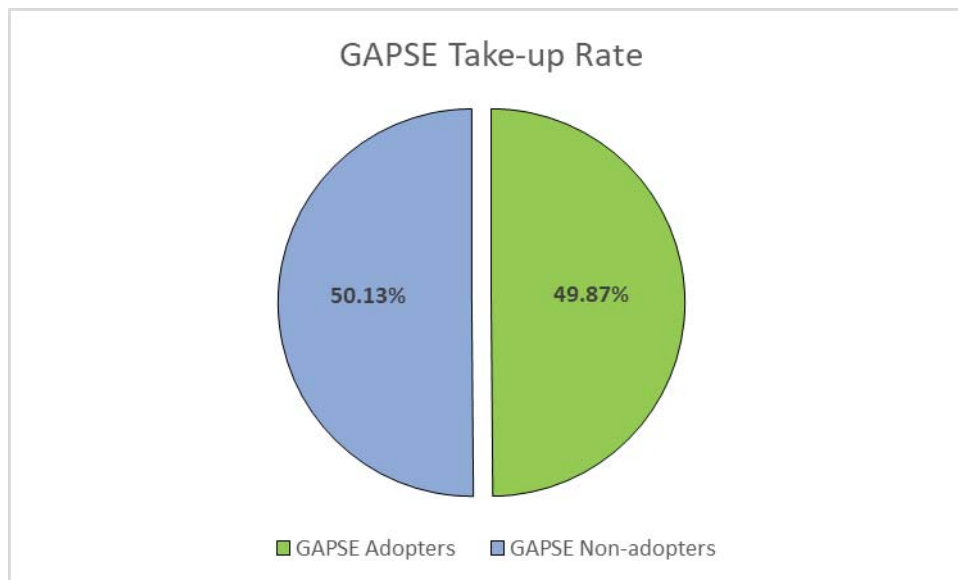
Figure 4.3 - Pie-chart illustrating the GAPSE take-up

By referring to previous studies which determined the GAPSE take-up rate over the years, a steady increase from 2011 to 2015 can be observed. Zammit (2011) found that GAPSE was used by a mere 18.5% of SMEs in 2011, which increased to 33% by 2013 (Zammit, 2011; Times of Malta, 2013). Therefore, the take-up rate of GAPSE being 49.9% in its last year of use (2015) reveals a steady increase over time which further suggests that the main reason why GAPSE had such a low take-up in its earlier years was lack of awareness and knowledge (Zammit, 2011).

Interestingly, all companies which used GAPSE in 2015 prepared their 2016 financial statements according to GAPSME, which indicates that companies which had opted for differential reporting through GAPSE transitioned to the newer GAPSME and did not revert back to IFRSs. All auditor interviewees stated similar statements to the following:

> "I have never encountered a client which was using GAPSE and then switched to IFRSs and not GAPSME."

> (Auditor interviewee 2)

Also notable is the fact that 130 companies which had not adopted GAPSE in the past converted to differential reporting through GAPSME adoption in 2016. This shift is what caused GAPSME to have such a high take-up when compared to GAPSE, with possible reasons for this being mentioned below.

4.2.3 – Reasons Why GAPSME Has a Higher Take-Up Rate Than GAPSE – Findings

The quantitative analysis was corroborated by the information derived from the interviews conducted. All participants clearly indicated that from what they have observed in the industry, GAPSME was seen in a more favourable light when compared to its predecessor, which supposedly should result in a higher percentage take-up. Below is a summary of the salient reasons provided for such widespread use of the GAPSME financial reporting framework.

The harmonisation of GAPSME's thresholds with the lowest EU thresholds imposed through the SAD widened the scope of GAPSME when compared to GAPSE, resulting in more companies being eligible to use GAPSME.

> "The thresholds before, under GAPSE, were 3/3 and the thresholds themselves were much lower. Now it is 2/3 and the thresholds are higher."

> (Auditor interviewee 2)

The fact that GAPSME is now the default framework for SMEs in Malta made it easier to adopt when compared to GAPSE, where a director's resolution was necessary to adopt the differential reporting framework. As stated by an auditor interviewee:

> "It is also easier to sell GAPSME due to the fact that it is now the default framework, therefore you do not really have to convince the client to take it."

(Auditor interviewee 1)

Another reason is that GAPSME is considered to be a significantly simplified framework, most notably through the removal of requirements to publish the Statement of Changes in Equity (SOCIE) and SOCF, which made it a more attractive option for SMEs. This is supported by an auditor interviewee which stated that:

> "The take-up of GAPSME is much more than GAPSE was because the financial reporting for small entities are much less onerous now than they were before."

(Auditor interviewee 2)

All interviewees highlighted the astronomical increase in IFRS complexity and compliance requirements in recent years as a main catalyst for GAPSME's popularity.

One interviewee stated that:

> "In recent times, IFRSs are becoming even more complex so there is added incentive to go for GAPSME. You have IFRS 9, 15 and 16 which are very complex, so the drive to choose GAPSME is higher than it was for GAPSE."

(Auditor interviewee 1)

This can also be observed through the following quotation which incorporates the opinion of most auditor interviewees regarding the timing of GAPSME's issuance.

> "Thank God GAPSME came when it came, because you have the small companies which have to create these complicated models, which would justify a higher fee and create a massive conflict."

(Auditor interviewee 5)

The MIA's push of GAPSME through advertising and numerous educational seminars was deemed to have partly targeted the lack of awareness which is said to have led to GAPSE's low take-up.

Finally, Maltese auditors were not completely comfortable with GAPSE, as it was considered to be a nationally developed inferior framework to IFRSs. An interviewee stated that this was "mainly due to it being purely cost based and lacking comparability." (Auditor interviewee 3).

4.2.4 – Discussion of Findings

At first glance, it is clear that the take-up of GAPSME in its first year of availability is much higher than the GAPSE take-up rates observed throughout its years in use. A possible reason for this is that in 2009, GAPSE was the first differential reporting framework in Malta and everyone was still engrained in IFRS thinking, with concerns being raised relating to the potential loss of IFRS expertise leading to SMEs being hesitant to embark on such a big transition. Meanwhile, GAPSME's issuance in 2016 caused much less of a stir as a differential reporting framework had already been available for a number of years.

A higher take-up for GAPSME was also expected as in its development, GAPSME addressed issues and concerns raised in relation to GAPSE. This automatically implies that while SMEs already using GAPSE were expected to easily transition to GAPSME, numerous SMEs which had not adopted GAPSE due to its flaws would consider adopting GAPSME due to its improvements.

GAPSME's broader scope, with a 14% increase in both revenue and total asset thresholds from its predecessor, lead to more SMEs being eligible to use the framework which can be considered as an obvious explanation for the differing take-up rates.

GAPSE's thresholds were also different to those stated by the CA with respect to abridged accounts. Given that SMEs' aim is to limit the information which they

submit to the ROC, SMEs were more focussed on producing abridged accounts rather than a simplified GAAP. Due to this reason, GAPSME might have appealed more to such a mentality due to its reduced presentation requirements together with its thresholds being aligned with those in the CA, also reducing confusion related to such matters through the removal of abridged accounts.

With GAPSME being established as the default framework for SMEs and advertised as a derived product of the SAD, this may have influenced users into acknowledging GAPSME as a more robust framework due to its affiliation with the EU. This contrasts greatly with the perception of GAPSE being an inferior framework primarily due to it being nationally developed and not set as the default framework for its target users.

Apart from clear efforts by the MIA to raise awareness about the benefits of adopting the GAPSME framework, the auditors themselves have significant influence on the framework decision made by their clients. Therefore, with the added complexities of IFRSs, auditors could have possibly recommended GAPSME in pursuit of their personal agenda and reduce the instances in which they would have to deal with unnecessary complications relating to leases and revenue, for example. This would not have been such a prevalent factor in relation to GAPSE as it was not considered to be much simpler from IFRSs at the time.

4.3 – RESEARCH OBJECTIVE 2: COMPANY-SPECIFIC FACTORS IMPACTING FRAMEWORK CHOICE

4.3.1 – Descriptive Analysis

The quantitative portion of this study comprises of a total of 25 independent variables, of both a continuous and categorical nature, which were analysed in relation to the dependent variable, which is the categorical variable relating to GAPSME adoption or not. The independent variables were identified following discussions with both industry experts and auditors to ensure that all variables which were deemed to possibly effect an SME's financial reporting framework choice were included. A detailed explanation of all the variables included, together with information as to how these were coded and imported into the SPSS statistical programme can be found in A.3.3.

Tables summarising the descriptive analysis of continuous and categorical variables are available in A4.1, which give the reader further insight into the nature and distribution of the data collected.

4.3.2 – Binary Logistic Regression – Findings

4.3.2.1 – Parsimonious model

Through comparison of all 6 regression methods available, the Backward: Conditional was deemed to produce the optimal parsimonious model. Such a decision was based on the number of significant predictors in the model (8), the percentage of correct classification of cases and model fit tests described below. The adopted 95% confidence interval implies p-values lower than 0.05 would indicate significance. The independent variable is said to better explain the dependent variable as the p-value decreases. The model choice is justified based

on the Goodness of fit indicators below. For original output tables, refer to Appendix Section A4.2.

A Nagelkerke R Square of 0.413 implies the significant variables explain 41.3% of the dependent variable and 41.3% of the dependent variable's variation is explained by the model. This was deemed to be an appropriate R^2 due to the nature and subjectivity of the dependent variable in question.

The Hosmer and Lemeshow Test result of 0.465 indicates the model should not be considered a poor fit as such a value is higher than 0.05 and therefore not deemed significant.

In addition to the above, the Classification table displays the percentage accuracy of classification, which at 87.2% suggests the model possesses a high level of predictive correctness.

Variable	B coefficients	Standard Error	P-Value	Odds Ratio
Company Size - Small	2.725	0.911	0.003	15.264
Debt/Equity ratio in 2016	-0.12	0.083	0.147	0.887
Auditor Size			0.018	
Auditor Size - Big 4	-1.139	0.476	0.017	0.32
Auditor Size - Mid-Tier	-1.016	0.475	0.032	0.362
Auditor Size - SMP	-1.008	0.394	0.011	0.365
Increase in Audit fees before GAPSME	0.932	0.445	0.036	2.539
Increase in Audit fees after GAPSME	3.554	1.13	0.002	34.965
Audit Report Lag	0.004	0.002	0.014	1.004
GAPSE use in the Past - No	-2.602	0.439	0.000	0.074
Investment in Subsidiaries - No	1.171	0.513	0.022	3.224
Constant	-0.753	1.092	0.49	0.471

Table 4.1 - Independent variables included in the parsimonious model

Table 4.1 illustrates the model output with the variables which were included in the final equation. From the P-values, which state the statistical significance of each independent variable, one can conclude that all independent variables contribute significantly to explaining the dependent variable, except for the Debt/Equity ratio in 2016 which exceeds the 0.05 significance level.

From the output of the model we can therefore establish clear links between the independent variables in the parsimonious model. The chance of a small

company adopting GAPSME is 15.264 times that of a medium company doing so. A company with a higher debt-equity ratio will most likely not adopt GAPSME, this being visible from the negative nature of the coefficient together with the odds ratio being less than 1.

A company audited by a big-4 audit firm is 68% less likely to adopt GAPSME than a company which is audited by a sole practitioner. SMEs audited by a mid-tier auditor and those audited by a Small-Medium Practitioner (SMP) are 63.8% and 63.5% less likely to adopt GAPSME than a sole practitioner audited company respectively. This therefore suggests that the smaller the practice of the auditor of a company is, the more likely it is to adopt GAPSME due to the observed inverse relationship between the two variables.

The odds of adopting GAPSME increase by a factor of 2.539 per percentage point increase in audit fees the company had experienced from 2012 till 2015, while the chances of GAPSME adoption increase by a staggering 34.965 times with every percentage point increase in audit fees between 2015 and 2016. This implies an increase in audit fees experienced between 2015 and 2016, when GAPSME could have been adopted for the first time, impacts greatly the probability of GAPSME adoption by an SME.

For every extra day of auditor report lag, a company is 0.4% more likely to adopt GAPSME. A company that had not adopted GAPSE in the past is 92.6% less likely to adopt GAPSME than a GAPSE adopter. This supports the opinion expressed by SME interviewees, which stated that GAPSME was seen as the obvious choice and the natural path to take after adopting GAPSE.

Interestingly, a company with no investments in subsidiaries is 3.2 times more likely to adopt GAPSME than a company which does have such investments.

The above findings also indirectly indicate what factors are prevalent in companies which are not likely to adopt GAPSME, when interpreting the odds ratio with respect to GAPSME non-adoption.

4.3.2.2 – The GAPSME adoption equation - Findings

Through simple substitution of the B-coefficients in the Table 4.1, the equation which gives the probability of a company adopting GAPSME can be deduced. A more detailed insight into the logistic regression equation can be found in Appendix Section A3.4.

$$Log(p/(1-p)) =$$

$$-0.753$$

$$+2.725(Company\ Size = Small)$$

$$-0.12(Debt - Equity\ ratio\ in\ 2016))$$

$$-1.139(Big\ 4\ Auditor)$$

$$-1.016(MidTier\ Auditor)$$

$$-1.008(SMP\ Auditor))$$

$$+0.932(Increase\ in\ audit\ fees\ before\ GAPSME)$$

$$+3.554(Increase\ in\ audit\ fees\ after\ GAPSME)$$

$$+0.004(Auditor\ report\ lag)$$

$$-2.602(GAPSE\ use\ in\ the\ past = No)$$

$$+1.171(Investment\ in\ Subsidiaries = No)$$

The above equation can be used to predict the probability of a company adopting GAPSME. This can be done by putting the predicted probability subject of the formula. This method is explained in Appendix Section A3.4.

Probability can be expressed as follows, with Exp denoting the exponent.

$$Exp[-0.753 + 2.725(Company\ Size = Small)$$
$$- 0.12(Debt - Equity\ ratio\ in\ 2016) - 1.139(Big\ 4\ Auditor)$$
$$- 1.016(Mid - tier\ Auditor) - 1.008(SMP\ Auditor)$$
$$+ 0.932(Increase\ in\ audit\ fees\ before\ GAPSME)$$
$$+ 3.554(Increase\ in\ audit\ fees\ after\ GAPSME)$$
$$+ 0.004(Audit\ report\ lag) - 2.602(GAPSE\ use\ in\ the\ past = No)$$
$$+ 1.171(Investment\ in\ subsidiaries = No)]$$

$$1 + Exp[-0.753 + 2.725(Company\ Size$$
$$= Small) - 0.12(Debt/Equity\ ratio\ in\ 2016)$$
$$- 1.139(Big\ 4\ Auditor) - 1.016(Mid - tier\ Auditor)$$
$$- 1.008(SMP\ Auditor)$$
$$+ 0.932(Increase\ in\ audit\ fees\ before\ GAPSME)$$
$$+ 3.554(Increase\ in\ audit\ fees\ after\ GAPSME)$$
$$+ 0.004(Audit\ report\ lag) - 2.602(GAPSE\ use\ in\ the\ past$$
$$= No) + 1.171(Investment\ in\ subsidiaries = No)]$$

A company was chosen at random from the dataset in order to test the equation and the model's predictive power. This company happened to be a small company audited by an SMP which had not used GAPSE in the past, had no investments in subsidiaries, had a debt/equity ratio of nil in 2016, experienced an increase of 285% in audit fees from 2012 to 2015 and 2% increase between 2015 and 2016 with the audit of its 2016 financial statements being signed 117 days after its financial year end.

The following values pertaining to the chosen company were therefore substituted into the above equation.

- Company Size = Small = 1
- Debt/Equity ratio in 2016 = 0
- Big 4 Auditor = 0
- Mid-tier Auditor = 0
- SMP Auditor = 1
- Increase in audit fees before GAPSME = 2.85
- Increase in audit fees after GAPSME = 0.02
- Audit Report Lag = 117
- GAPSE use in the past = No = 1
- Investment in Subsidiaries = No = 1

$$\frac{Exp[\,-0.753\,+\,2.725(1)\,-\,0.12(0)\,-\,1.139(0)\,-\,1.016(0)\,-\,1.008(1)\,+\,0.932(2.85)\,+\,3.554(0.02)\,+\,0.004(117)\,-\,2.602(1)\,+\,1.171(1)]}{1+Exp[\,-0.753\,+\,2.725(1)\,-\,0.12(0)\,-\,1.139(0)\,-\,1.016(0)\,-\,1.008(1)\,+\,0.932(2.85)\,+\,3.554(0.02)\,+\,0.004(117)\,-\,2.602(1)\,+\,1.171(1)]}$$

The predicted probability of GAPSME adoption of this company is equal to 0.936727 (14.80465/15.80465 = 0.936727), this suggesting the company with the characteristics denoted above is 93.7% probable to be a GAPSME adopter. This is in line with the estimated probability calculated by the model. The high probability is also justified as the company chosen was in fact a GAPSME adopter in 2016.

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4.3.2.3 – Relationships identified through non-parametric testing

Associations between variables were also tested through non-parametric tests such as the Spearman's Correlation, Chi-Square test of independence and Mann-Whitney Test.

Correlations

			CurrentYearD ebtEquityRati o	IncreaseinAu ditFeesAfterG apsme	AuditReportL ag	AgeofCompa ny
Spearman's rho	CurrentYearDebtEquityRa tio	Correlation Coefficient	1.000	.079	-.031	.115[*]
		Sig. (2-tailed)	.	.117	.535	.021
		N	399	399	399	399
	IncreaseinAuditFeesAfter Gapsme	Correlation Coefficient	.079	1.000	-.100[*]	-.045
		Sig. (2-tailed)	.117	.	.045	.370
		N	399	399	399	399
	AuditReportLag	Correlation Coefficient	-.031	-.100[*]	1.000	.063
		Sig. (2-tailed)	.535	.045	.	.212
		N	399	399	399	399
	AgeofCompany	Correlation Coefficient	.115[*]	-.045	.063	1.000
		Sig. (2-tailed)	.021	.370	.212	.
		N	399	399	399	399

*. Correlation is significant at the 0.05 level (2-tailed).

Table 4.2 - Results of the Spearman's Correlation test

The Chi-Square test of independence was used to determine relationships between two categorical variables. Relationships were considered significant if the p-value was less than 0.05 and the Cramer's V statistic was used in order to gauge the strength of the link between variables.

Auditor size was found to be significantly related to the GAPSME adoption. With a p-value of <0.0005 and a Cramer's V of 0.250 indicating a moderately strong correlation between the two, implying the size of the auditor of an SME has a significant influence on whether the company will adopt GAPSME or not. This is also visible by the inclusion of auditor size in the parsimonious model. 87.4% of sole practitioner clients use GAPSME while only 57.5% of Big 4 clients adopt it, indicating smaller auditors deal much more with GAPSME. Almost half of GAPSME adopter's financial statements were audited by sole practitioners while only 7% were audited by Big 4 firms.

With a p-value of <0.0005 and Cramer's V of 0.286, company size was found to have a significant relationship with GAPSME adoption, as small SMEs are considered more likely to adopt GAPSME than medium SMEs are. GAPSME was adopted by 82.7% of sampled small companies and 16.7% of medium companies.

Medium companies were found to be more likely to have consolidated accounts, with a weak correlation identified between company size and the preparation of consolidated financial statements. While 16.7% of medium companies published consolidated financial statements, a mere 1.3% of small companies did the same.

The Mann-Whitney test was used to expose any significant difference in the distribution of continuous variable scores for different groups of a categorical variable.

Auditor report lag scores are distributed significantly differently between firms that have adopted GAPSME and those that have not. This indicates that GAPSME did have an effect on the duration of SME audits. (U=14497, z=-2.314, p=0.021)

Through non-parametric testing, additional information regarding the relationships between independent variables and the dependent variable was deduced, supporting the model findings. Also, several independent variables which were not included in the model and which did not provide a statistically significant result through individual non-parametric testing against the dependent variable cannot be considered influential in an SME's financial reporting framework choice. Such variables include:

- Growth in assets
- Current ratios
- External Finance
- Audit report qualifications in previous years
- Age of company
- Industry
- Asset valuation policy
- Government grants

4.3.3 – Discussion of Findings

A small company being significantly more likely to adopt GAPSME is to be expected, as GAPSME requirements for small companies are much simpler when compared to IFRSs, while those for medium companies are only slightly simplified.

This implies that small companies are more incentivised to adopt GAPSME through the substantial requirement reductions when compared to medium companies. Another explanation for this is that most smaller SMEs are audited by sole practitioners and SMPs which are expected to be less versed in IFRSs and would therefore push GAPSME adoption in order to avoid the complexities which IFRSs incorporate.

Alternatively, Big-4 audit firms are considered to be well versed in IFRSs and therefore more likely to push IFRSs. Such firms also would not want to lose IFRS knowledge, which is said to be an undesirable side effect of widespread GAPSME usage, as they will still need to use IFRSs in relation to their larger and PIE clients.

Audit fees were found to have a significant impact on the adoption of GAPSME, with a positive correlation between an increase in audit fees and the likelihood of GAPSME adoption. This may be interpreted as a company which has experienced an increase in audit fees pre-2016 being more incentivised to adopt GAPSME in an attempt to limit the audit fee increase.

Another way of interpreting this would be that this intrinsically implies that a company which adopted GAPSME in its first available year (2016) experienced an increase in audit fees. While this conflicts with what was explained by interviewees, it is possible that due to 2016 being the first year of use, several auditors marketed GAPSME as a new introduction which would entail certain additional costs thus justifying an increase in audit fees charged to 2016 financial statement audit engagements.

A reason why this was not considered impactful, and therefore did not warrant a mention by respondents could be that such increases were reversed when such additional costs were no longer being incurred or the magnitude of this increase in audit fees for 2016 GAPSME financial statements was not deemed to be an alarming one.

Auditor report lag was also found to significantly explain the dependent variable, with every additional day of report lag marginally increasing the chance that GAPSME will be adopted. This implies that companies which adopted GAPSME in its first year of issuance experienced a longer audit report lag. A possible reason for this occurrence is that most of the companies which would have opted for GAPSME are not bound by strict deadlines, as it was found that the main use of audited financial statements for most SMEs is simply to abide by ROC filing requirements. This could lead to such companies having a longer auditor report lag, not directly because they have opted to use GAPSME, but because the auditor would prioritise clients with stricter deadlines.

GAPSE adoption and GAPSME adoption being significantly related is expected, as one would find it easier to switch from one differential reporting framework to another rather than switching from the robustness of IFRSs to the much simplified GAPSME.

It could also be anticipated that companies with investments in subsidiaries are less likely to adopt GAPSME. The main reasoning behind such an expectation is that these companies are part of a group, where due to the low consolidation thresholds, a high majority would need to consolidate, which as explained by an auditor interviewee, reduces the attractiveness of GAPSME adoption for such SMEs.

Medium companies were expected to be more likely preparers of consolidated financial statements, with another specific reference to the small group consolidation thresholds, where having a medium company as part of a group already exceeds such thresholds and thus demands consolidation.

4.4 – RESEARCH OBJECTIVE 3: GAPSME FEEDBACK BY AUDITORS AND SME REPRESENTATIVES

4.4.1 – Pragmatic Benefits of GAPSME - Findings

After 3 years of first-hand experience with GAPSME, respondents related to the below reasons as to why GAPSME has proven to be such a vital option for SMEs.

IFRSs have become so complex that demanding such detailed reporting from SMEs is nonsensical and a regulatory overkill. This sentiment is clearly observable through the following quotation:

> "IFRSs are a lot more complex and detailed such as financial instruments which includes valuations and models which are very expensive. Therefore, forcing such small firms to produce these models is considered overkill and most SMEs are not compatible with such models."

(Auditor interviewee 3)

Additionally, many SMEs simply produce financial statements due to statutory obligations and taxation purposes. This reality was stated by an SME respondent, where he explained that:

> "The audited financial statements are mainly for external stakeholders. Business decisions are made during the year and cannot be postponed to when you have the audited accounts in front of you, therefore you still have to have real-time record keeping procedures to be able to take informed decisions based on the situation at that point in time."

(SME interviewee 1)

The users of SME financial statements are also different from those of large listed companies, therefore through the concept of differential reporting, SME financial statements are said to be adept to SME financial information users while IFRSs are more appropriate to users of larger entities. An auditor interviewee went on to elaborate that:

> "I think that IFRSs are overkill for smaller entities, especially considering the users of SME financial statements. When you have regulated or large entities, the users include regulators, shareholders and investors with huge balances, therefore you need a detailed and comprehensive annual report with a lot of disclosure and explanations of material balances. If you look at SMEs, these are normally limited companies with a small number of shareholders, often family members."

<div align="right">(Auditor interviewee 3)</div>

4.4.2 – Concerns Relating to GAPSME's Perceived Inferiority - Findings

All auditor interviewees stated that they do not consider GAPSME to be an inferior framework for the purpose it is meant to fulfil, being the financial reporting of SMEs.

> "GAPSME is specifically adapted and tailored to the needs of the firms which are able to use it. For those firms, it is not considered inferior. They are simpler and more user friendly but not inferior for the purpose they set out to achieve."

<div align="right">(Auditor interviewee 4)</div>

This is supported by the fact that GAPSME financial statements are not intrinsically considered to present a higher audit risk when compared to IFRS financial statements, as the audit risk of a company is not influenced by the accounting framework used but by the situation of each individual client and the same audit procedures have to be carried out according to International Auditing standards, irrespective of the framework used.

An interviewee did however consider IFRS financial statements to contain a higher audit risk due to the following reason:

> "The new IFRSs, in their complexity, are perhaps more open to manipulation and misinterpretation than the simpler GAPSME framework."

<div align="right">(Auditor interviewee 3)</div>

However, a number of concerns were raised regarding the quality of GAPSME financial statements when compared to IFRSs.

Whilst acknowledging that for SME financial statements, GAPSME and IFRSs give similar levels of information, another interviewee suggested that people knowledgeable in accounting will notice the difference by stating:

> "Many are used to having a set of IFRS statements, so you will go through GAPSME financial statements expecting to find a certain level of detail and things such as the SOCF and SOCIE. You are disappointed when looking at GAPSME financial statements and not having such information readily available."

(Auditor interviewee 1)

Many auditor participants compared GAPSME to its predecessor and stated that while GAPSE was truly considered to be inferior to IFRSs, the same cannot be said with respect to GAPSME.

> "With GAPSE for example, there was this perception that it is a standard that is of inferior quality, the fact that it wasn't made the default framework speaks for itself."

(Auditor interviewee 1)

GAPSME is therefore considered a robust framework which is respected by the Maltese accountancy profession. This is clearly observable through the following quotation.

> "I have not yet encountered a fellow practitioner who has had something really bad to say about the framework, actually I think the profession was really looking forward to it. Overall, I think it hit its goals and was taken up in a positive light."

(Auditor interviewee 4)

While always having room for fine-tuning and improvements, it was found that 3 years down the line, GAPSME has proven to be a step in the right direction for SME financial reporting in Malta. This contrasts greatly with the preliminary expectations of accounting professionals interviewed by Dimech (2016), where 11 out of 12 respondents stated that GAPSME was considered a step in the wrong direction (Dimech, 2016).

4.4.3 – The Costs of GAPSME Adoption - Findings

All three SME interviewees, which had prepared their financial statements according to both GAPSE and GAPSME, indicated that no significant costs were incurred directly related to the switch from GAPSE to GAPSME.

Many SMEs did however expect a reduction in audit fees due to GAPSME financial statements being considerably shorter and simpler in nature. Such expectations can be summarised through the following quotation, where an SME respondent stated that:

> "To be honest I did slightly expect a small reduction in audit fees as it is a move to a supposedly simpler framework, but the auditor explained the fact that the audit work and testing necessary is still the same, as GAPSME's simplifications were focussed on presentation rather than recognition and measurement."
>
> (SME interviewee 3)

The above SME expectation is also in line with the preliminary expectations of accounting practitioners, as Dimech (2016) found that:

> "It will probably be the case that SME owners will want answers why financial statements are now significantly smaller and may also ask for fee reductions due to the lower amount of content."
>
> (Dimech, 2016, pp. 47)

Auditors stated that generally, the small reduction in audit work necessary did not warrant a reduction in audit fees and thus audit fees neither increased nor decreased directly due to adherence to GAPSME. An explanation for this is that:

> "Fees aren't really based on the framework you are using but trends, market and competitive forces are the main drivers of audit fees charged. Certainly, the fees have not gone down due to GAPSME's introduction, and to my knowledge, no professional has tried to decrease audit fees charged to clients … Fees are dictated by the market and regulation cannot really affect this."
>
> (Auditor interviewee 4)

Although when observed in isolation, GAPSME did not result in direct cost savings for SMEs which adopted it, auditor interviewees highlighted a significant indirect cost saving experienced by GAPSME adopters when compared to the alternative preparation of IFRS financial statements.

> "The distinction in fees is mainly that if you were to use IFRSs, the fees would have surely increased due to a significant increase in necessary work. Whereas if you are using GAPSME, you have remained in the same situation which indirectly suggests that by using GAPSME you have saved money."

(Auditor interviewee 1)

4.4.4 – Who Influences the Financial Reporting Framework Decision in Practice? - Findings

Auditors were said to greatly influence their client's financial reporting framework decision. This was also stated by an SME participant through the following quotation:

> "Due to the nature of the work and the people involved, the auditor has a huge influence over the framework decision."

(SME interviewee 2)

While larger audit practices tend to produce information brochures with a brief explanation together with the pros and cons of both GAPSME and IFRSs as adopted by the EU, smaller practices stated that most of their clients directly request the auditor to suggest the most beneficial framework given their circumstances. The latter situation was further explained by a sole practitioner interviewee, which stated that:

> "You also find those who leave the choice to you as they do not really care about the financial statements and do not make use of them themselves. Most are purely interested in the least costly approach, which is obviously GAPSME."

(Auditor interviewee 5)

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SME respondents also expressed similar reasoning to that mentioned in the quotation above, with all of them suggesting that GAPSME did not really impact their business due to their lack of interest in statutory financial statements for internal purposes. An SME interviewee stated that:

> "The accounts prepared by the accountant, who is also the auditor, is not really meant for the directors' use but for external stakeholders mainly the banks, tax department and the ROC. The directors prefer the information available through the management accounts as it is easier to follow."

<div align="right">(SME interviewee 1)</div>

This finding is in line with findings observed through a UK study, where management accounts were considered to be more useful for internal purposes than statutory financial statements, with the former being used by 81.8% of SMEs and 70.6% using the latter (Collis and Jarvis, 2002).

Another reason why SMEs may have not experienced much changes in relation to GAPSME adoption is:

> "In our case, there aren't many complex transactions that require major differences between one framework and another. This may be due to the fact that GAPSME has simplified greatly its presentation requirements but has not really changed much of the recognition and measurement ones."

<div align="right">(SME interviewee 3)</div>

Thus, from the above findings, one can deduce that SME owners seem indifferent with regards to what reporting framework the statutory financial statements follow and tend to simply refer to their auditor to identify the cheapest option. This agrees with what was found by Dimech (2016), as many SME owners were expected to either be indifferent, while those which internally made use of statutory financial statements would be worse off due to the less information available (Dimech, 2016).

While 11 out of 12 practitioners interviewed by Dimech (2016) expected banks to be worse off due to GAPSME, particularly due to the lack of SOCF and disclosures in general, findings of this study found that GAPSME's effect on

banks was minimal. Reasons for this include the fact that banks can always demand supplementary information and could therefore still obtain the same level of information included in IFRS financial statements, with an auditor interviewee stating:

> "For bankers, I think nothing really changed as we still provide the SME with a cashflow statement and the bank requires it anyway, so no real change has occurred."

> (Auditor interviewee 4)

Another reason, suggested by both auditors and SME representatives, is the fact that banks do not base their credit-granting decision purely on information included in financial statements, but mainly refer to future projections which also corresponds to Dimech's findings (Dimech, 2016). The following quotations describe respondents' experiences in dealing with banks:

> "When you have an overdraft, banks will always require a set of audited financial statements and when we sent them GAPSME financial statements, they were deemed to be sufficient. However, when it comes to obtaining a loan, they require more information including forward-looking projections of cashflows, IS and Statement of Financial Position (SOFP)."

> (SME interviewee 1)

> "I would not say that banks care about the framework, these are just formalities. With material long-term loans, they require information which goes over and above that in the financial statements, which are mainly used to get a first impression of the financial position of the applicant."

> (SME interviewee 2)

Therefore, the main concerns raised in Dimech's thesis regarding banks being expected to be worse off due to the lack of information and specifically the SOCF in GAPSME financial statements were not observed 3 years down the line (Dimech, 2016). It can also be concluded that banks are not as influential with respect to the accounting framework decision as they were perceived to be, with GAPSME financial statements being accepted by banks.

Another user group which could possibly influence the reporting framework choice are creditors. However, findings deduced from interview responses suggest creditors, specifically those dealt with by SMEs, do not require or use financial statements in making their credit-granting decision, with the "current ratio and going concern of the company" being more important. Creditors' lack of demand for financial statement information is also in line with what Dimech's preliminary study concluded, as relationships and past experience being highlighted as the main criteria considered in Maltese creditor decision making (Dimech, 2016).

An auditor did however point out that:

> "I doubt how much creditors actually check the financial statements before dealing with a client. It happens mostly in specific cases when foreign suppliers are involved, as they tend to request financial statements beforehand."

(Auditor interviewee 4)

Therefore, it may be concluded that the major influence in the financial reporting framework decision comes from auditors, with owners, banks and creditors generally being indifferent as to which framework is adopted.

4.4.5 – The Main Drawbacks of GAPSME - Findings

One of the main drawbacks of GAPSME mentioned by auditor respondents was regarding the low group consolidation thresholds, illustrated in table 4.3 below.

Small Groups		
	Net	**Gross**
Balance Sheet total	≤ €4,000,000	≤ €4,800,000
Total revenue	≤ €8,000,000	≤ €9,600,000
Average number of employees	≤ 50	≤ 50

Table 4.3 - Small Group Consolidation GAPSME thresholds. Source: https://www.gvzh.com.mt/malta-publications/gapsme-general-accounting-principles-small-medium-enterprises/).

These thresholds are considered too low and reduce the benefits experienced by SMEs which use GAPSME for their individual financial statements but are still forced to prepare consolidated financial statements.

An auditor interviewee elaborated by stating that:

> "We are also encountering many instances where you often have to consolidate as the thresholds are easily exceeded. Maybe there may be an argument to raise the thresholds for group consolidations … The main argument is that GAPSME is fine for the individual subsidiaries, but when you are forced to consolidate it may feel like you have lost this benefit."

(Auditor interviewee 1)

While another emphasized the gravity of the situation by stating:

> "The small group thresholds are too low, we had cases where they choose IFRSs simply because of this consolidation."

(Auditor interviewee 5)

The most noticeable concern was raised with respect to the exclusion of the SOCF and SOCIE from GAPSME's presentation requirements. This exclusion was not appreciated by a number of auditors and SMEs as many deemed such statements to be useful and necessary in both preparation and analysis of a set of financial statements. The following quotations provide an explanation as to why these statements are considered useful:

> "I do not understand why the SOCIE was removed as a requirement and I certainly do not agree with this. It shows the movement of the company's worth and may be used as an internal reconciliation exercise."

(SME interviewee 2)

> "Regarding the SOCIE and SOCF removal, I personally do not agree with them being removed from the presentation requirements. I personally still produce them for my clients as the SOCIE is important to understand the IS and SOFP while the SOCF is important for internal purposes as cash is the lifeblood of the business."

(Auditor interviewee 4)

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The above concerns are aligned with the preliminary expectations found through Dimech's study in 2016, where the SOCF exclusion was listed by many as a step backwards while others stated that the exclusion of the SOCIE should not be underestimated (Dimech, 2016).

GAPSME's simplifications were also criticised by auditors for being purely presentational and not focussing on the more important recognition and measurement principles.

A specific reference to such an instance was made by a particular respondent, where he explained that:

> "In every seminar that I attended, a headache which many others were encountering was the infamous shareholders' or related party loans. Where GAPSE only required a disclosure and the amount, in GAPSME, if it is long-term and there is a schedule of repayment, you have to establish the commercial value of the loan and discount accordingly. In this respect, GAPSME is very close to IFRSs and this is a very common scenario in SMEs, as most funds tend to come from the shareholder which is also the ultimate beneficiary owner."

(SME interviewee 2)

The concerns deduced from interviewees suggest that although GAPSME is an improvement on its predecessor and is considered to be a respected and robust framework, improvements can always be made in order to further facilitate SME financial reporting in Malta.

4.4.6 – Discussion of Findings

Although the Maltese accountancy profession is considered to be well versed in IFRS regulation, the recently issued standards will prove to be a challenge even for the most IFRS financially literate professional. When trying to arrive at the value of certain figures such as leases, revenue and financial instruments, one would need certain underlying data which is not readily available, especially in the specific case of smaller SMEs. An example of such data includes the credit

rating of counter-parties which is required for provisions under IFRS 9, where very few Maltese SMEs, if any, are rated by credit rating agencies.

Therefore, when adhering to IFRS requirements, practitioners can be expected to encounter multiple dead ends where the required data cannot be reliably collected. The same can be said for IFRSs' discounting requirements, where the data necessary to reliably arrive at an appropriate discount rate is not attainable, which in turn leads to excessive judgements and assumptions. GAPSME has been received as a beneficial framework as it simplifies such requirements while still providing a true and fair view given the size and nature of eligible companies.

As IFRSs are mainly directed towards larger firms listed on capital markets, where the shareholders (owners) are not the managers, this does not align with the situation of SMEs, which tend to be owner-managed. Therefore, in the case of SMEs, the principal-agent problem and information asymmetry between the directors and the shareholders rarely need to be addressed, as the owners of most SMEs are involved in the day-to-day running of the company. This is therefore the main reason why most SME owners do not perceive audited financial statements as useful and opt for the lesser of two evils in order to meet their reporting obligations, which through responses was clearly identified as GAPSME.

Another reason why GAPSME is considered beneficial to SMEs is due to the high level of financial illiteracy which Maltese SME owners often possess. Providing such owners with a complex set of IFRS financial statements will surely overwhelm the average man on the street. For most SME owners, the business is simply a matter of revenue less cost equals profit, as such people tend to simply care about the bottom-line figures and how much money they have pocketed.

Therefore, GAPSME provides a much simpler and straight forward set of financial statements which still provides owners and other external users with the necessary information, but in a much simpler format. This may also encourage SME owners to go through the audited GAPSME financial statements and perform some simple analysis, which already makes GAPSME financial

statements more useful for SMEs than IFRSs can ever be and may increase the financial literacy of SME owners over time.

Findings also highlight the fact that GAPSME is not perceived to be an inferior framework. This can also be deduced from comparison of the higher GAPSME take-up rate with that of its predecessor, which intrinsically implies that GAPSME is a more respected and highly thought of framework than GAPSE was, which in turn also corroborates with many interviewees emphasizing their negative opinion on GAPSE and the improvements which GAPSME has provided.

GAPSME may not have been considered as an inferior framework as it relieves auditors and practitioners of a huge workload when compared to what they would be required to do under IFRSs. Therefore, when comparing the disadvantages of GAPSME with the impracticality and complexity of IFRSs, GAPSME is considered to be a more simplistic and realistic way of preparing SME financial statements.

The MIA may have also influenced the perception of many professionals with respect to GAPSME by intentionally advertising it as an improvement of the Maltese differential reporting framework which is also in line with the SAD. Thus, although the SAD had limited influence on the GAPSME framework, it was advertised in such a way, to highlight the harmonisation between the two.

Interestingly, it was found that there were no real transitional costs incurred by companies adopting GAPSME for the first time. This is to be expected as the change, especially for companies which used GAPSE beforehand, would not demand large restructuring of accounting processes within the SMEs. The fact that audit fees remained stagnant through GAPSME adoption is understandable, as in practice, fees are not dependent on which financial reporting framework has been used, but on the resources, such as chargeable hours, which the audit of that particular company requires. Any small fluctuations in the time spent to conduct an audit is not going to immediately translate into a change in fees charged, even as auditors mostly tend to steadily increase their fees over time in line with their competitors.

The cost savings brought about through GAPSME were perhaps not as obvious as the owners would have hoped for, as actual fees charged had not decreased in monetary terms. However, when one considers the exponential increase in IFRS audit fees over the last few years, the fact that GAPSME audit fees have remained fairly constant indicates that GAPSME adoption will save the SME money on their audit engagement, as the gap between the expense of a GAPSME audit and an audit of the other optional framework is widening.

Auditors were found to influence the framework decision of their clients to a high extent. This is expected as most SMEs have their financial statements prepared and audited by the same professional or firm. SMEs, especially those smaller in size, are not realistically going to analyse the pros and cons of both framework alternatives and will ask their auditor to identify the optimal choice for their situation. This is also observable in the fact that owners were not considered to be avid users of the audited financial statements.

The auditor is also expected to choose what is best for the client and for themselves and will mainly push GAPSME in order to reduce the complexities which they themselves have to deal with.

Preliminary concerns, such as those raised through Dimech (2016), regarding banks not accepting GAPSME financial statements, seems to be unfounded, especially with regards to short-term credit such as bank overdraft. Such concerns did however materialise in relation to foreign banks, which were found to demand IFRS financial statements, however cases where SMEs deal in loans from foreign banks are expected to be few and far in between.

Also, the banks' perceived use of financial statements in its credit-granting decision making seems to be overstated, as financial statement information is overshadowed by the importance of forward-looking projections for such institutions.

Maltese suppliers are not considered to be one of the main users of SME financial statements, which implies their lack of influence on the reporting framework decision is expected. Similar to banks, foreign suppliers are more likely to

demand financial statements before selling on credit terms, however such trading relations are rare in the context of Maltese SMEs.

The main drawbacks listed by interviewees, derived through their use of GAPSME over the past 3 years, included the over-simplification of presentation requirements, such as the removal of the SOCIE and especially the SOCF. As interviews found that GAPSME financial statements are widely considered to be merely a simpler way of satisfying their presentation obligations imposed by the ROC. Therefore, could the owners' and auditors' concerns relating to the reduced presentation requirements be mainly due to constant comparison with IFRSs, with the focus being on statements which both were used to having at their disposal under IFRS. This could be due to the Maltese profession's mentality, which has been engrained in IFRSs for so long that many are still reluctant to fully simplify the financial reporting for SMEs.

The above may also suggest that GAPSME's simplifications were mainly directed to the wrong areas, with many suggesting improvements through the further simplification to recognition and measurement principles, in specific instances such as the discounting of shareholder loans which are quite prevalent in the Maltese SME population.

Regarding concerns relating to the small group consolidation thresholds, such quantitative thresholds are not solely determined by the MIA but also restricted on an EU level. If such quantitative thresholds cannot be increased in order to reduce the likelihood that SMEs will be asked to consolidate, the MIA should consider the introduction of qualitative criteria which must be met before a small group is required to consolidate.

4.5 – CONCLUSION

This chapter included an accumulation of the findings obtained throughout this study, with clear reference to the objectives the study set out to achieve. A discussion and interpretation of these findings was also included, providing the writer's take on the information obtained and comparison with his interpretations together with any relevant literature.

Chapter 5

Conclusion

5.1 – INTRODUCTION

This chapter will conclude the study, including a summary of the study and its findings clearly showing how the research objectives have been met, a number of recommendations and areas of potential further research. The structure of this chapter is illustrated in Figure 5.1.

5.1 - INTRODUCTION

5.2 - SUMMARY

- •5.2.1 - Summary of Research
- •5.2.2 - Summary of Main Findings

5.3 - RECOMMENDATIONS

- •5.3.1 - Widening of Small Group Consolidation Criteria
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5.4 - AREAS FOR FURTHER RESEARCH

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5.5 - CONCLUDING REMARKS

Figure 5.1 - Chapter 5 Overview.

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5.2 – SUMMARY

5.2.1 – Summary of Research

This study set out to fulfil its 3 main research objectives, through which a comprehensive feedback exercise and analysis of the GAPSME take-up rate would be achieved together with the identification of relationships between company specific factors and an entity's accounting framework choice.

The research process included an in-depth review of both foreign and local prior literature, as well as the collection and analysis of primary data, both of a quantitative and qualitative nature.

Quantitative research comprised of the collection of financial statement information for 399 companies for financial years spanning from 2012 to 2016. This was then statistically analysed through a binary logistic model, together with non-parametric testing, in order to identify and discuss any statistically significant correlations that were identified.

Qualitative research involved the conduction of 8 in-depth semi-structured interviews with 5 auditors, with each audit firm size being represented, and 3 SME representatives. Through categorisation of responses, interviewee opinions, feedback and recommendations were documented and discussed.

5.2.2 – Summary of Main Findings

The main findings obtained through this study can be directly related to each of the research objectives as follows.

Objective 1	• Assess the take-up of GAPSME by eligible Maltese SMEs

In satisfaction of the first research objective, this study concluded that the take-up rate of GAPSME in 2016, which was also the first year GAPSME was available for use, was approximately 82.4%, with 98% of companies being eligible to use GAPSME. When compared to its predecessor, GAPSE, GAPSME seems to have been more widely adopted mainly due to the following reasons mentioned by both sets of interviewees:

-   Wider scope due to less restrictive quantitative and qualitative thresholds;
-   GAPSME being the default framework for SMEs while GAPSE was not;
-   Significant disclosure simplifications which reduced the SME reporting burden greatly;
-   The significant increase in IFRS complexity in the last four years; and
-   GAPSME being a more respected framework by the profession.

Objective 2	• Assess whether specific company factors have an impact on the accounting framework applied by SMEs (GAPSME vs IFRSs as adopted by the EU)

A binary logistic model was used to identify any relationships between 25 independent company variables and the dependent variable (use of GAPSME). The parsimonious model, with an R^2 of 41.3% and 8 statistically significant independent variables was deemed to reliably estimate the expected probability

of a company's adoption of GAPSME or not. The factors which were found to significantly influence the framework choice of a company included:

- Company Size;
- Auditor Size;
- Increase in Audit Fees before GAPSME adoption;
- Increase in Audit Fees after GAPSME adoption;
- Audit Report Lag;
- GAPSE adoption in the past; and
- Investment in Subsidiaries.

Through odds ratio analysis, the main relationships between the above variables and the probability of GAPSME adoption were deduced and summarised as follows:

- A small company is more likely to adopt GAPSME than a medium company. Auditor size was also found to significantly influence framework choice, as companies audited by smaller audit practices are more inclined towards GAPSME;
- Companies which had opted for GAPSE in the past are much more likely to adhere to GAPSME than non-GAPSE adopters; and
- Companies with investments in subsidiaries were identified less likely to choose GAPSME.

These findings therefore directly satisfied the second objective of this study, with the equation obtained through the statistical model enabling the estimation of GAPSME adoption probability by simply substituting figures related to the 8 variables listed above.

Objective 3

- Obtain feedback by auditors and SMEs regarding GAPSME, together with suggested improvements and their opinions on the framework 3 years after its issuance for use

Interviews proved instrumental in understanding the perception of GAPSME after being used in practice for three years.

Some main findings extracted from both auditor and SME interviewees include:

- Smaller audit practices deal more with SMEs than the larger Big-4 audit firms.

- Differential reporting is considered beneficial by auditors, especially considering the financial illiteracy amongst SME owners and the low internal importance of audited financial statements for most SMEs.

- GAPSME is a respected framework amongst the Maltese accountancy profession and is not considered inferior to IFRSs for the purpose they set out to achieve. This contrasts with the auditors' opinion on GAPSE.

- Audit risk is not contingent on the reporting framework used but on company specific factors. This also negates the misconception that audit work has significantly decreased due to GAPSME's issuance.

- The main drawbacks of GAPSME stated by auditors included the absence of the SOCF and SOCIE together with the low small group consolidation thresholds, with SME representatives highlighting the former two exclusions.

- SME owners appreciated GAPSME's simplicity although they rarely use statutory financial statements for internal purposes, in favour of the more practical management accounts.

- Banks were said to have not experienced significant changes due to GAPSME as they still demand supplementary information and tend to base their credit-granting decisions on information other than that attainable from audited financial statements, such as future projections.

- Creditors were not considered avid users of SME financial statements, except in the case of foreign creditors where the lack of detailed information may have proved detrimental.

- GAPSME did not directly cause a decrease in audit fees, however the stagnant nature of audit fees suggests GAPSME adoption translated into indirect cost savings.

5.3 – RECOMMENDATIONS

Based on the above findings, this study makes the following recommendations:

5.3.1 – Widening of Small Group Consolidation Criteria

The MIA should consider widening the criteria which oblige small groups to consolidate. If expanding the quantitative thresholds is not possible due to EU restrictions, a qualitative threshold could prove useful in further reducing SMEs' reporting burden.

5.3.2 – Recognition and Measurement Simplifications

While the majority of opinions relating to GAPSME were positive, a recurring concern regarding the lack of recognition and measurement simplifications warrants the MIA's attention, which should discuss a possible revision of GAPSME's requirements with relation to specific areas highlighted by participants in this study. Furthermore, SMPs and sole practitioners should be included in such discussions due to their higher exposure to SME clients and valuable feedback concerning entities which fall in the smaller GAPSME threshold size spectrum.

5.3.3 – Improve SME Owner Financial Literacy

The lack of statutory financial statement use for internal purposes reinforces the need to further educate SME owners and provide them with the necessary knowledge to unlock the full benefits of financial statements. The potential impact of MIA intervention is evident, as most interviewees highlighted MIA's educational seminars and informative sessions as a main contributor to GAPSME's success.

5.4 – AREAS FOR FURTHER RESEARCH

The results of this dissertation have identified the following areas which warrant further research:

5.4.1 - Follow-up Research

In light of this study's limitations, a GAPSME feedback exercise in 3 – 5 years would prove useful to gauge the perceptions of main stakeholders and provide an opportunity for comparison. This would be specifically relevant if IFRSs continue to increase in complexity and any revision to aspects of GAPSME, such as those recommended above, are issued.

5.4.2 – Study Focussing on Other Main Stakeholders

A purely qualitative study, with multiple interviews from each of the stakeholder groups not in the scope of this study, such as banks, tax authorities and the MFSA, would provide a more holistic perspective of GAPSME.

5.5 – CONCLUDING REMARKS

The GAPSME framework is a testament to a successful locally developed differential reporting framework. The Maltese profession took the plunge and deviated from IFRSs, which were all it had known at that point. An element of trial and error also played its part, as GAPSE had numerous flaws which, with hindsight, set it up for failure. However, GAPSME has proven to be a much-improved version which defied most expectations.

Moving forward, both the MIA, as the developers of the GAPSME framework, and the main users of GAPSME financial statements must work in unison to ensure that the optimal framework for all stakeholders is established.

"It takes both sides to build a bridge." – Fredrik Nael

Appendices

A3.1 - MARGIN OF ERROR CALCULATION

Margin of Error = zσp

For a 95% degree of confidence, z = 1.96.

σp is the standard error which is maximised when p = 0.5.

$$\sigma p = \sqrt{\frac{p(1-p)}{n}\left(\frac{N-n}{N-1}\right)}$$

For a population (N) = 47000, the maximum value of the standard error σp is:

$$\sigma p = \sqrt{\frac{(0.5)(0.5)}{n}\left(\frac{47000-n}{47000-1}\right)}$$

$$\sigma p = 0.023\sqrt{\frac{47000-n}{n}}$$

With a maximum margin of error set to be 5%, then n can be found as follows:

$$z\sigma p = (1.96)(0.023)\sqrt{\frac{47000-n}{n}} = 0.05$$

$$47000 = 123.34n$$

$$n = 381$$

The target sample size to achieve a maximum margin of error of 5% is therefore 381 observations.

A3.2 - DATA NORMALITY – SHAPIRO-WILK TEST

Tests of Normality

	Kolmogorov-Smirnov[a]			Shapiro-Wilk		
	Statistic	df	Sig.	Statistic	df	Sig.
GrowthinAssets	.456	399	.000	.074	399	.000
PreviousYearDebtEquityRatio	.432	399	.000	.146	399	.000
CurrentYearDebtEquityRatio	.423	399	.000	.174	399	.000
PreviousYearCurrentRatio	.468	399	.000	.052	399	.000
CurrentYearCurrentRatio	.437	399	.000	.175	399	.000
IncreaseinAuditFeesBeforeGapsme	.317	399	.000	.398	399	.000
IncreaseinAuditFeesAfterGapsme	.354	399	.000	.498	399	.000
AuditReportLag	.208	399	.000	.905	399	.000
AgeofCompany	.096	399	.000	.917	399	.000
ProportionofRevaluedAssets	.530	399	.000	.091	399	.000
GovernmentGrantorTaxCredit2016	.513	399	.000	.028	399	.000
GrantorCreditAmountprevious2years	.513	399	.000	.027	399	.000

a. Lilliefors Significance Correction

Table A3.1 - Results of Tests of Normality carried out on all continuous variables

An assessment of normality was carried out, with specific reference to the Shapiro-Wilk test, which is deemed more appropriate for smaller sample sizes. The hypotheses tested through both the above tests are as follows:

H_0: Variable is normally distributed

H_1: Variable is not normally distributed

As illustrated in the output table above, with specific reference to the Sig. columns which represent the P-values, all variables have been found to be significant at the 0.05 level of significance, with an output of (.000).

This results in H_1 being accepted and therefore concluding that all the continuous variables do not follow a normal distribution. The Kolmogorov-Smirnov test, which is an alternative test of normality for larger samples, also produced similar results to the Shapiro-Wilk test, further confirming the non-normality of the continuous data. The implications of this finding also determined the nature of statistical tests which were used, as non-parametric tests were selected as the most appropriate tests to analyse the quantitative data collected.

A3.3 – EXPLANATION OF VARIABLES

Variable	Measurement Scale	Explanation
Use of GAPSME	Dependent	'0' if the company is not using GAPSME, '1' if the company is using GAPSME.
Foreign Shareholders	Nominal	'0' if the main shareholder or holding company is foreign, '1' if they are Maltese.
Company Size	Nominal	'1' if the company qualifies as small, '2' if it qualifies as medium. GAPSME thresholds were used to determine company size.
Eligibility to use GAPSME	Nominal	'0' if the company is not eligible to use GAPSME, '1' if it is eligible to use GAPSME. This was determined considering GAPSME size thresholds and whether the company qualifies as a PIE.
Growth in Assets	Metric	Gives the % growth in total assets of the company between 2012 and 2015.
External Finance	Nominal	'0' if the company has no external bank finance, '1' if the company does have external bank finance. Bank loans and bank overdraft were considered to be bank finance.
Previous year Debt/Equity Ratio	Metric	The company's Debt/Equity ratio for 2015. Debt was considered to be bank loans and bank overdraft.
Current year Debt/Equity Ratio	Metric	The company's Debt/Equity ratio for 2016. Debt was considered to be bank loans and bank overdraft.
Previous year Current Ratio	Metric	The company's Current ratio for 2015. This was calculated as Current Assets/Current Liabilities.
Current year Current Ratio	Metric	The company's Current ratio for 2016. This was calculated as Current Assets/Current Liabilities.
Auditor Size	Nominal	'1' if the company's auditor is a Big 4 audit firm, '2' if the auditor is a Mid-tier audit firm, '3' if the auditor is a Small/Medium Practitioner (SMP) and '4' if the auditor is a Sole Practitioner.
Increase in Audit Fees before GAPSME	Metric	The % increase in audit fees charged between 2012 financial statements and 2015 financial statements.
Increase in Audit Fees after GAPSME	Metric	The % increase in audit fees charged between 2015 financial statements and 2016 financial statements.
Qualifications in Previous Years	Nominal	'1' if the company received a Qualified Opinion between 2012 and 2015, '2' if the company did not receive a Qualified Opinion between 2012 and 2015, '3' if the company received an Emphasis of Matter paragraph between 2012 and 2015 and '4' if the company received a Disclaimer of Opinion between 2012 and 2015.
Audit Report Lag	Metric	Time in days between the 2016 financial year end and the 2016 financial statement auditor's report signature date.
Age of Company	Metric	Time in years between the registration date of the company and the end of 2016.
Industry	Nominal	The industry which the company primarily operated in according to its Memorandum and Articles. Nominal coding was used to categorise companies according to industry.
Industry Regulated or Non-Regulated	Nominal	'1' if the industry which the company primarily operates in is regulated, '2' if the industry is non-regulated. Regulated industries encountered only included Insurance Companies.
Asset Valuation Policy	Nominal	'1' if the company prepared their financial statements according to the Historical Cost convention, '2' if the company used both historical cost and revaluation valuation methods (Mixture).
Proportion of Revalued Assets	Metric	The % of assets which were revalued. This was calculated as Revalued assets/Total assets.
Shareholders are Directors	Nominal	'0' if the main shareholder is also a director of the company, '1' if the main shareholder is not a director.
Consolidated Accounts	Nominal	'0' if the company had not published consolidated financial statements, '1' if the company had also published consolidated financial statements.
GAPSE used in the past	Nominal	'0' if the company had not prepared financial statements according to GAPSE between 2012 and 2015, '1' if the company had prepared financial statements according to GAPSE between 2012 and 2015.
Government Grant/Tax Credit 2016	Metric	The amount in euros of any government grant or tax credit disclosed in the company's 2016 financial statements.
Government Grant/Tax Credit previous 2 years	Metric	The amount in euros of any government grants or tax credits disclosed in the company's 2015 and 2014 financial statements.
Investments in Subsidiaries	Nominal	'0' if no investment in subsidiaries were disclosed in the company's 2016 financial statements, '1' if any investment in subsidiaries were disclosed in the company's 2016 financial statements.

Table A3.2 - An explanation of all variables used in statistical analysis.

A3.4 - DESCRIPTION OF BINARY LOGISTIC REGRESSION MODEL

In order to understand better the model used, below is a mathematical interpretation of a logistic regression. The success probability in this study refers to GAPSME adoption, which is also the dependent variable.

Let $Y, X_1, \ldots, X_q$ be random variables. The logistic or logit model which refers directly to the success probability, p is defined by

$$\mathbb{E}\big[Y|X = (x_1, x_2, \ldots, x_q)\big] = p\big(x_1, \ldots, x_q\big) = \frac{\exp(\beta_0 + \beta_1 x_1 + \cdots + \beta_q x_q)}{1 + \exp(\beta_0 + \beta_1 x_1 + \cdots + \beta_q x_q)} \qquad (1)$$

where $\beta_0, \ldots \beta_q$ are unknown regression co-efficients.

A transformation of $p(x)$ such that the right-hand side of equation (1) is linear, is the logit function which is expressed by

$$logit\big(p(x)\big) = \log\left(\frac{p(x)}{1 - p(x)}\right) = \beta_0 + \beta_1 x_1 + \cdots + \beta_q x_q \qquad (2)$$

where $p(x) = p(x_1, \ldots, x_q)$ is the probability of success.

The logistic regression model in equation (2) has linear form for the logit of this probability. Also, the right-hand side of the equation gives the logarithm of the odds from which the predicted probabilities may be calculated. Based on these probabilities, a subject or object may then be assigned to one of the two categories of the response variable. (Tabachnick et al., 2007 as cited in Montebello, 2010) (Cohen J. et al., 2003 as cited in Montebello, 2010)

After having established the above equation, the following will serve as guidance as to how the parameters included in the Linear Regression model should be interpreted.

Consider a binary response variable Y, and a single explanatory variable X. Then the logistic regression model will be given by:

$$\mathbb{E}[Y|X = x] = p(x) = \frac{exp(\alpha + \beta x)}{1 + exp(\alpha + \beta x)},$$

where the relationship between p(x) and x is clearly non-linear. Now, any probability must be greater than or equal to zero and less than or equal to 1. This is illustrated clearly in the simulation of the actual model found in Section 4.3.2.2.

A3.4.1 – Assumptions and Limitations of the Logistic Regression

The Logistic regression also has the following notable underlying assumptions. (Tabachnick et al., 2007 as cited in Montebello, 2010) (Laerd Statistics, 2018)

1) The Logistic regression is assumed to have a binary dependent variable.

2) There must be a linear relationship between the continuous independent variables and the logit transformation of the dependent variable.

3) A Logistic regression requires a large sample size and the maximum likelihood estimation is used to estimate its parameters. Large sample sizes enable asymptotic normality, efficiency and consistency of maximum likelihood estimators, whereas smaller samples could be responsible for high standard errors and un-reasonably high logistic coefficients.

4) Categories of the binary dependent variable and all nominal independent variables should be mutually exclusive and exhaustive.

5) There should be no multicollinearity between the independent variables.

A3.4.2 – Evidence of Logistic Regression Assumption Satisfaction

The first assumption is automatically satisfied as the Use of GAPSME, which is the dependent variable, is a binary variable with two categories, 0 - No and 1 - Yes.

The second assumption was tested using the Box-Tidwell (1962) procedure which is to be performed only on the continuous variables. All continuous independent variables included in the parsimonious model were transformed into their natural logs, generating the following four new variables:

- ln_ Current Year Debt Equity Ratio
- ln_ Increase in Audit Fees Before GAPSME
- ln_ Increase in Audit Fees After GAPSME
- ln_ Audit Report Lag

Interaction terms between the continuous variables and their respective natural log transformed variables were then created and entered into the binomial logistic regression procedure together with the dependent variable, the continuous and categorical variables included in the final parsimonious model in order to run the Box-Tidwell (1962) procedure.

Variables in the Equation

		B	S.E.	Wald	df	Sig.	Exp(B)
Step 1[a]	Size(1)	2.339	.919	6.480	1	.011	10.371
	AuditorSize	.381	.173	4.835	1	.028	1.464
	CurrentYearDebtEquityRatio	-.106	.265	.160	1	.689	.899
	IncreaseinAuditFeesBeforeGapsme	1.464	1.126	1.688	1	.194	4.321
	IncreaseinAuditFeesAfterGapsme	5.013	7.882	.405	1	.525	150.363
	AuditReportLag	.063	.022	8.207	1	.004	1.065
	GAPSEusedinthepast(1)	-2.124	.460	21.338	1	.000	.119
	InvestmentinSubsidiaries(1)	1.259	.637	3.902	1	.048	3.521
	CurrentYearDebtEquityRatio by ln_Debt	.001	.097	.000	1	.994	1.001
	IncreaseinAuditFeesBeforeGapsme by ln_Audit_Fee_Before	.370	1.235	.090	1	.765	1.448
	IncreaseinAuditFeesAfterGapsme by ln_Audit_Fee_After	2.315	5.317	.190	1	.663	10.128
	AuditReportLag by ln_Audit_Report_Lag	-.009	.003	7.742	1	.005	.991
	Constant	-4.101	1.412	8.432	1	.004	.017

a. Variable(s) entered on step 1: Size, AuditorSize, CurrentYearDebtEquityRatio, IncreaseinAuditFeesBeforeGapsme, IncreaseinAuditFeesAfterGapsme, AuditReportLag, GAPSEusedinthepast, InvestmentinSubsidiaries, CurrentYearDebtEquityRatio * ln_Debt , IncreaseinAuditFeesBeforeGapsme * ln_Audit_Fee_Before , IncreaseinAuditFeesAfterGapsme * ln_Audit_Fee_After , AuditReportLag * ln_Audit_Report_Lag .

Table A3.3 - Box-Tidwell (1962) procedure output.

Table A4.2 highlights the rows that contain the interaction terms and their respective Sig. column values. As recommended, a Bonferroni correction based on all terms (including the intercept) in the model was carried out.

Therefore, since there are 13 terms in this model, we divide the p-value at which statistical significance is accepted – that is, $p < 0.05$, by the number of terms in the model. As such, the new level at which statistical significance would be accepted becomes $p < 0.003846$ (i.e., 0.05/13). At this new level of significance, as all p-values exceed this level of significance, one can conclude that all continuous independent variables are linearly related to the logit of the dependent variable.

The third assumption is satisfied as the parameter estimates for the variables included in the parsimonious model were reasonable and their standard errors were small. The sample size taken (399) is also large enough with a sufficient margin of error of less than 5% (A3.1).

The fourth assumption is satisfied through the goodness of fit measures of the final model (A4.4), such as the Hosmer-Lemeshow test which is estimated by the chi-square statistic. This together with the Nagelkerke R^2 and overall percentage of correctness indicate a good model fit.

The fifth assumption was satisfied through a Spearman's Correlation and Chi-Square tests, which indicate any multi-collinearity between variables. Where multi-collinearity was identified, one of the variables was excluded from the model (A4.3).

A3.4.3 – Explanation of The Odds Ratio

In addition to the interpretation of the parsimonious model equation, the logistic regression output also includes the odds ratio, which can also be interpreted.

An odds ratio higher than 1 indicates a positive relationship between the independent and dependent variable, while a negative relationship is identified through an odds ratio which is lower than 1. This can therefore be used to analyse the direction of predicted movements of the dependent variable with relation to a change in the independent variable. A positive or negative relationship between the explanatory variables and the dependent variable can also be confirmed through the positive or negative nature of the coefficient (Complete Dissertation, 2019).

The odds ratio for categorical variables must always be interpreted in terms of the group which is coded the highest. Therefore, where the company size categorical variable is coded as small = 1 and medium = 2, the odds ratio is interpreted in terms of the small company being more or less likely to adopt GAPSME when compared to the higher coded medium company (Complete Dissertation, 2019).

The odds ratio for continuous variables is interpreted in terms of a unit increase in the continuous variable. An example of this is found in the case of auditor report lag, calculated in days. Here, the odds ratio should be interpreted as the change in likelihood of GAPSME adoption, with an increase in one unit (one day) of audit report lag (Complete Dissertation, 2019).

The odds ratio in itself can be interpreted in two main ways. An odds ratio of 3.224 for the investment in subsidiaries explanatory variable, which is coded as no = 0 and yes = 1, can either be explained as a company with no investment in subsidiaries is 3.224 **more** likely to adopt GAPSME than a company with investment in subsidiaries, or in terms of percentage increase in probability, where a company with no investment in subsidiaries would be (3.224 – 1) 222.4% **more** likely to adopt GAPSME than a company which has investment in subsidiaries.

An odds ratio which is less than 1, such as that of GAPSE used in the past (0.074), coded as no = 0 and yes = 1, is easier interpreted in percentage terms, where in this case, a company which had not adopted GAPSE is (1-0.074) 92.6% **less** likely to adopt GAPSME than a company which had used GAPSE.

A3.5 - DESCRIPTION OF NON-PARAMETRIC TESTS

Before developing the Binary Logistic model, the tests explained below were conducted as a form of multivariate analysis in an attempt to identify any significant association between variables which could be used to improve the explanatory power of the model itself and ensure the best results were obtained from the financial statement data collected. These tests resulted in certain variables being excluded from the model, as explained in Section 4.4.2.1.

All the tests used were of a non-parametric nature. These are tests that are carried out if parametric tests cannot be employed due to the non-normal distribution of the data. Normality was tested using the Shapiro-Wilk test, the results of which can be found in Section 4.4.1.4.

A3.5.1 – Spearman's Correlation Test

The Spearman's correlation test is used to investigate any association between two continuous variables. Through the Spearman correlation coefficient one can also interpret the magnitude of the association together with whether the relationship between the variables concerned is of a positive or negative nature.

H_0 = There is no association between the variables

H_1 = There is an association between the variables

The null and alternative hypotheses of the Spearman's correlation test are stated above, which imply when the p-value (Sig.) is less than the 0.05 level of significance, the null hypothesis (H_0) is rejected and the alternative hypothesis (H_1) is accepted, thus indicating an association between the variables. Two-tailed tests were executed in order to ensure all possible correlations were tested. (Laerd Statistics, 2018)

A3.5.2 - Chi-Square Test of Independence

The Chi-Square test is used to check for any relationships between two nominal (categorical) variables.

H_0 = There is no association between the variables

H_1 = There is an association between the variables

The null and alternative hypotheses of the Chi-Square test are stated above. The null hypothesis (H_0) is rejected when the p-value (Asymptotic Significance) is less than the 0.05 level of significance, which in turn accepts the alternative hypothesis (H_1) and indicates an association between the tested variables. Once again, two-tailed tests were run in order to ensure all possible correlations were tested.

As the Chi-Square test does not provide information relating to the strength of the association found, the Cramer's V value is used to provide an estimate of the magnitude of such association. The Cramer's V value is found in the Symmetric Measures table and is interpreted through the table below. (Laerd Statistics, 2018)

Magnitude of Association	Value of Cramer's V
Low	$0.1 < V < 0.3$
Moderate	$0.3 \leq V < 0.5$
High	$V \geq 0.5$

Table A3.4 - Interpretation of Cramer's V values. Source: (Cohen, 1988, pp.223)

A3.5.3 - Mann-Whitney U Test

The Mann-Whitney test is used to identify whether a continuous variable is differently distributed between 2 groups of a categorical variable. The null and alternative hypotheses of the Mann-Whitney test are stated below.

H_0 = There is no significant difference in the distribution of scores across groups

H_1 = There is a significant difference in the distribution of scores across groups

If the p-value (Sig.) is lower than the 0.05 significance level, the null hypothesis (H0) is rejected which implies the alternative hypothesis (H1) is accepted. This would therefore indicate that the concerned continuous variable scores are not equally distributed equally between the 2 categories in question and can lead to interpretations as to what relationship between the 2 tested variables may have caused this uneven distribution of values. (Laerd Statistics, 2018)

A3.6 – STATISTICAL TEST RESULTS JUSTIFYING VARIABLE EXCLUSIONS FROM THE MODEL

A3.6.1 – Eligibility of GAPSME Correlation vs Dependent Variable

Crosstab

			EligibilitytouseGAPSME No	EligibilitytouseGAPSME Yes	Total
UseofGAPSME	No	Count	8	69	77
		% within UseofGAPSME	10.4%	89.6%	100.0%
		% within EligibilitytouseGAPSME	100.0%	17.6%	19.3%
		Adjusted Residual	5.8	-5.8	
	Yes	Count	0	322	322
		% within UseofGAPSME	0.0%	100.0%	100.0%
		% within EligibilitytouseGAPSME	0.0%	82.4%	80.7%
		Adjusted Residual	-5.8	5.8	
Total		Count	8	391	399
		% within UseofGAPSME	2.0%	98.0%	100.0%
		% within EligibilitytouseGAPSME	100.0%	100.0%	100.0%

Table A3.5 – Cross-tabulation showing the association between Eligibility of GAPSME and Use of GAPSME. ($\chi^2(1) = 34.139$, $p<0.0005$, Cramer's V = 0.293)

Chi-Square Tests

	Value	df	Asymptotic Significance (2-sided)	Exact Sig. (2-sided)	Exact Sig. (1-sided)
Pearson Chi-Square	34.139[a]	1	.000		
Continuity Correction[b]	29.056	1	.000		
Likelihood Ratio	27.023	1	.000		
Fisher's Exact Test				.000	.000
Linear-by-Linear Association	34.053	1	.000		
N of Valid Cases	399				

a. 1 cells (25.0%) have expected count less than 5. The minimum expected count is 1.54.

b. Computed only for a 2x2 table

Table A3.6- Output table of Eligibility of GAPSME VS Use of GAPSME Chi-Square test.

Symmetric Measures

		Value	Approximate Significance
Nominal by Nominal	Phi	.293	.000
	Cramer's V	.293	.000
N of Valid Cases		399	

Table A3.7 - Output table showing the Cramer's V value for the correlation between the Eligibility to use GAPSME VS Use of GAPSME.

A3.6.2 – Correlations Amongst Continuous Independent Variables

Correlations

		PreviousYear DebtEquityRatio	CurrentYear DebtEquityRatio	PreviousYear CurrentRatio	CurrentYear CurrentRatio	GovernmentG rantorTaxCre dit2016	GrantorCredit Amountprevio us2years	ProportionofR evaluedAsset s
Spearman's rho	PreviousYearDebtEquityRatio							
	Correlation Coefficient	1.000	.896**	-.107*	-.112*	-.005	-.005	-.044
	Sig. (2-tailed)	.	.000	.033	.026	.919	.919	.379
	N	399	399	399	399	399	399	399
	CurrentYearDebtEquityRatio							
	Correlation Coefficient	.896**	1.000	-.056	-.091	-.001	-.001	-.042
	Sig. (2-tailed)	.000	.	.263	.069	.980	.980	.408
	N	399	399	399	399	399	399	399
	PreviousYearCurrentRatio							
	Correlation Coefficient	-.107*	-.056	1.000	.860**	.044	.044	.026
	Sig. (2-tailed)	.033	.263	.	.000	.379	.379	.605
	N	399	399	399	399	399	399	399
	CurrentYearCurrentRatio							
	Correlation Coefficient	-.112*	-.091	.860**	1.000	.050	.050	.016
	Sig. (2-tailed)	.026	.069	.000	.	.323	.323	.746
	N	399	399	399	399	399	399	399
	GovernmentGrantorTaxCredit2016							
	Correlation Coefficient	-.005	-.001	.044	.050	1.000	1.000**	.225**
	Sig. (2-tailed)	.919	.980	.379	.323	.	.	.000
	N	399	399	399	399	399	399	399
	GrantorCreditAmountprevious2years							
	Correlation Coefficient	-.005	-.001	.044	.050	1.000**	1.000	.225**
	Sig. (2-tailed)	.919	.980	.379	.323	.	.	.000
	N	399	399	399	399	399	399	399
	ProportionofRevaluedAssets							
	Correlation Coefficient	-.044	-.042	.026	.016	.225**	.225**	1.000
	Sig. (2-tailed)	.379	.408	.605	.746	.000	.000	.
	N	399	399	399	399	399	399	399

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

*Table A3.8- Spearman Correlation table showing correlations between continuous independent variables, with specific reference to those marked with '**', which are significant at the 0.01 level.*

A4.1 – DESCRIPTIVE ANALYSIS

A4.1.1 – Continuous Variables

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
GrowthinAssets	399	-1.0000	328.5011	2.247762	23.4572778
PreviousYearDebtEquityRatio	399	.00	68.77	.7076	4.13104
CurrentYearDebtEquityRatio	399	.00	44.55	.5114	2.64885
PreviousYearCurrentRatio	399	.00	31563.17	133.4710	1650.53750
CurrentYearCurrentRatio	399	.00	2359.76	30.6248	166.10545
IncreaseinAuditFeesBeforeGapsme	399	-1.00	8.00	.1011	.56965
IncreaseinAuditFeesAfterGapsme	399	-1.00	2.00	.0385	.20873
AuditReportLag	399	2.00	748.00	250.1103	111.31100
AgeofCompany	399	3.91	50.27	18.1746	8.89552
ProportionofRevaluedAssets	399	.00	.95	.0089	.07841
GrantorCreditAmountprevious2years	399	0	996626	2617.84	49934.746
GovernmentGrantorTaxCredit2016	399	0	914725	2412.57	45838.778
Valid N (listwise)	399				

Table A4.1 - Descriptive statistics relating to continuous variables.

A4.1.2 – Categorical Variables

Variable	Category	Frequency	Percentage
Use of GAPSME (Dependent Variable)	No	77	19.30%
	Yes	322	80.70%
Foreign Shareholders	No	340	85.20%
	Yes	59	14.80%
Company Size	Small	387	97.00%
	Medium	12	3.00%
Eligibility to use GAPSME	No	8	2.00%
	Yes	391	98.00%
External Finance	No	263	65.90%
	Yes	136	34.10%
Auditor Size	Big 4	40	10.00%
	Mid-Tier	38	9.50%
	SMP	138	34.60%
	Sole Practitioner	183	45.90%
Industry (only incl. most frequent)	Real Estate	63	15.80%
	Construction	28	7.00%
	Holding Company	17	4.30%
	Retail	72	18.00%
	Manufacturing	29	7.30%
	Investment Company	32	8.00%
	Consultancy	23	5.80%
	Technological Services	17	4.30%
	Catering	18	4.50%
	Entertainment	10	2.50%
Industry Regulation	Regulated	3	0.80%
	Non-Regulated	396	99.20%
Asset Valuation Policy	Cost	393	98.50%
	Mixture	6	1.50%
Main Shareholders are Directors	No	112	28.10%
	Yes	287	71.90%
Consolidated Accounts	No	392	98.20%
	Yes	7	1.80%
GAPSE used in the past	No	200	50.10%
	Yes	199	49.90%
Investment in Subsidiaries	No	370	92.70%
	Yes	29	7.30%
Qualifications in Previous Years	Yes	29	7.30%
	No	322	80.70%
	Emphasis of Matter	46	11.50%
	Disclaimer of Opinion	2	0.50%

Table A4.2 - Descriptive statistics relating to categorical variables.

A-19

A4.1.3 – Categorical Variable Frequency Graphs

The graphs below illustrate the distributions of observations relating to categorical variables across their groups.
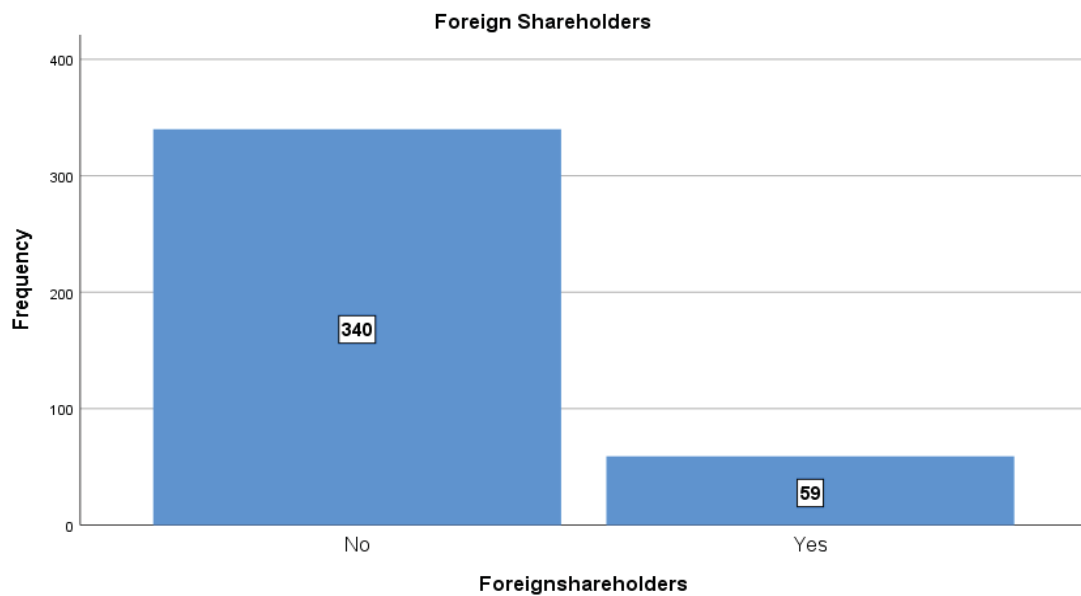

Figure A4.1 - Distribution of observations of the Foreign Shareholders variable.
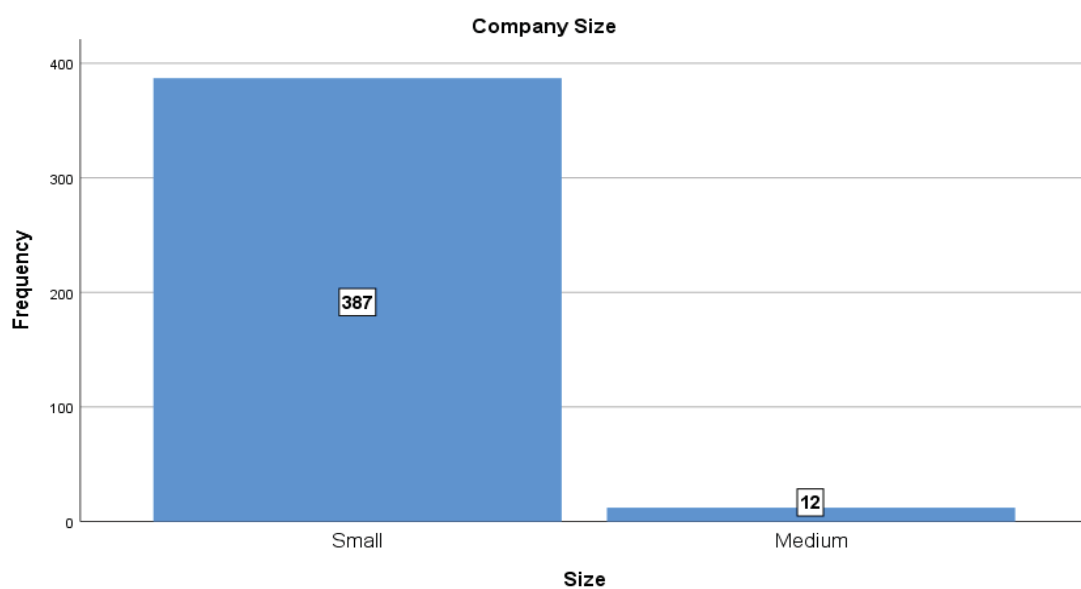
Figure A4.2 - Distribution of observations of the Company Size variable.

Eligibility to use GAPSME
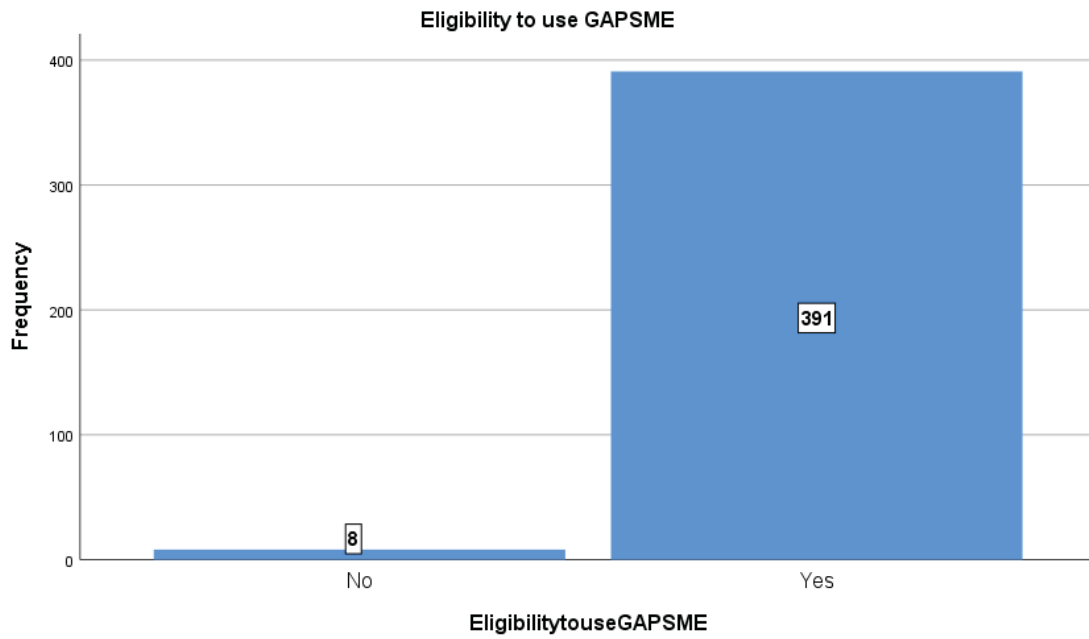
Figure A4.3 - Distribution of observations of the Eligibility to use GAPSME variable.

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Use of GAPSME
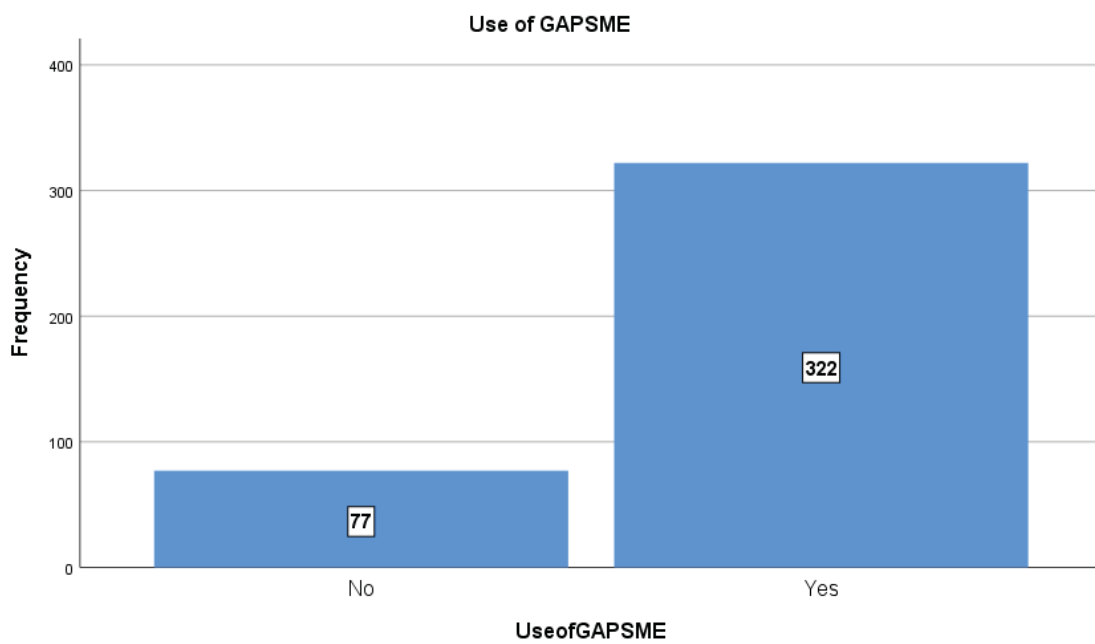
Figure A4.4 - Distribution of observations of the GAPSME adoption variable.

A-21
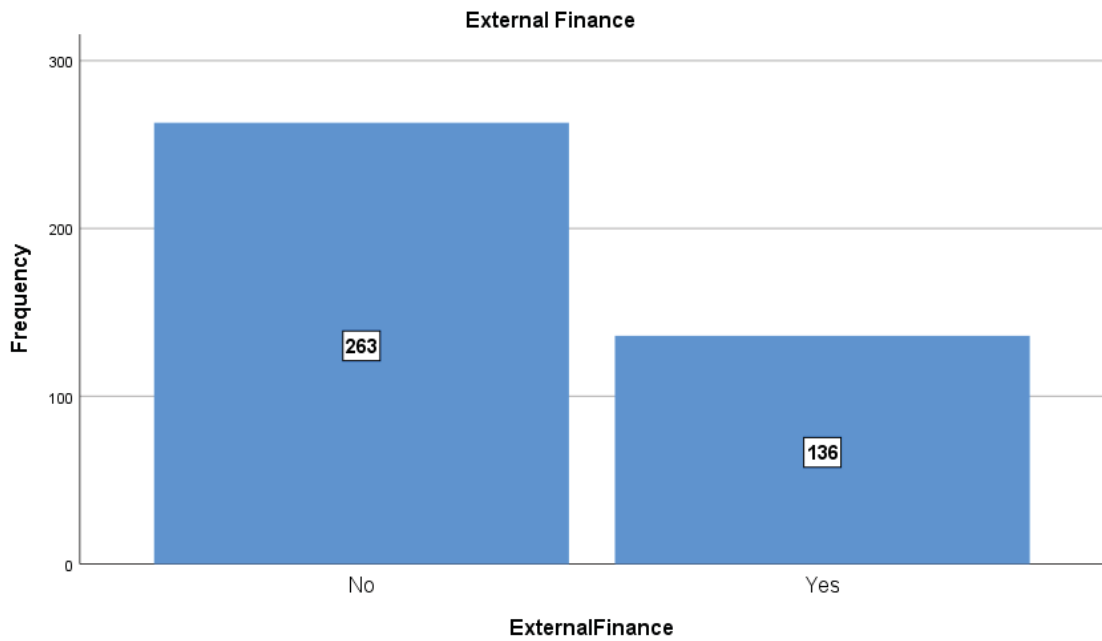
External Finance

Figure A4.5 - Distribution of observations of the External Finance variable.
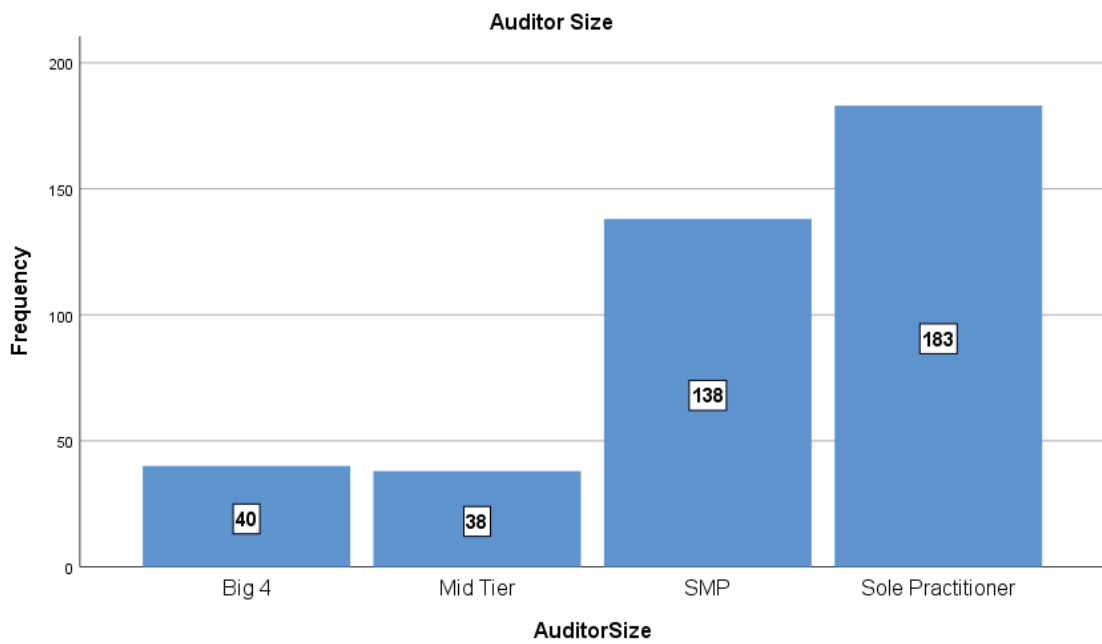
Auditor Size

Figure A4.6 - Distribution of observations of the Auditor Size variable.
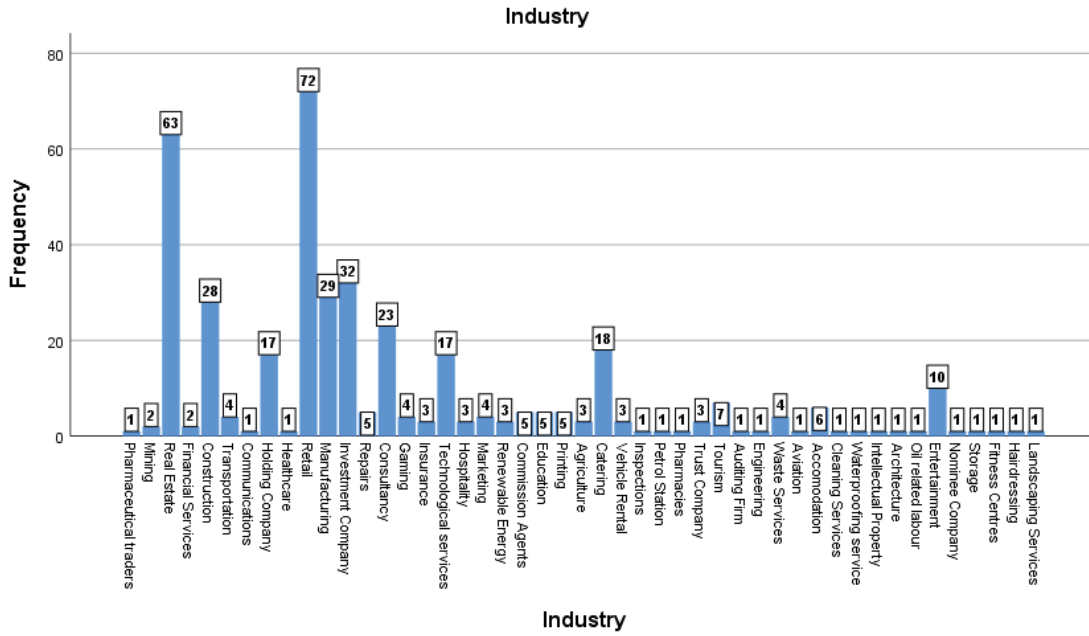
Figure A4.7 - Distribution of observations of the Industry variable.
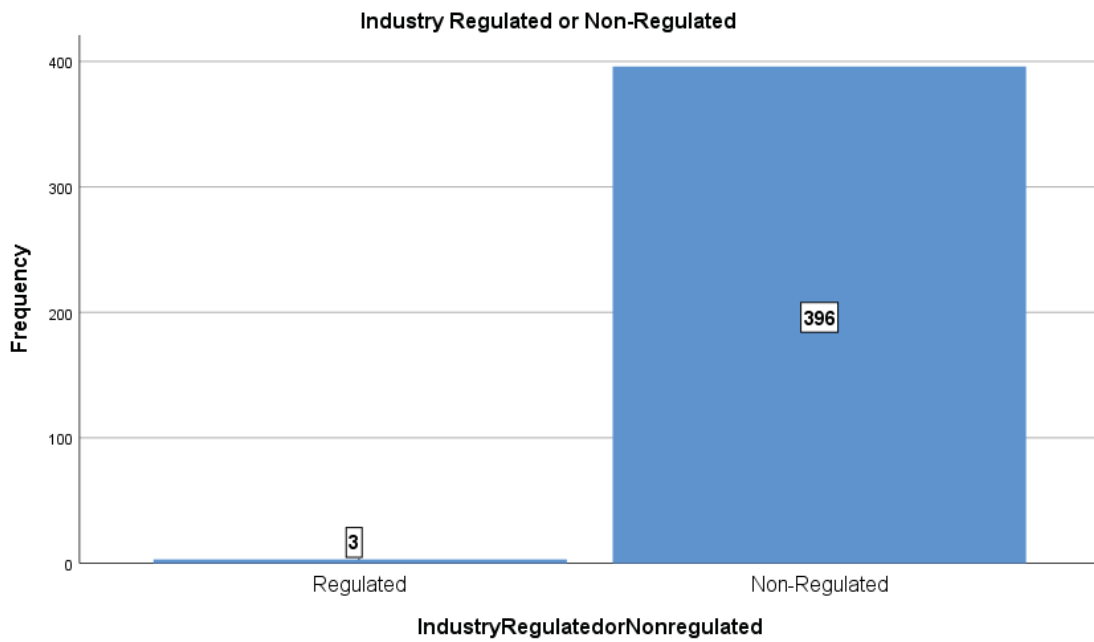
Figure A4.8 - Distribution of observations of the Industry Regulation variable.
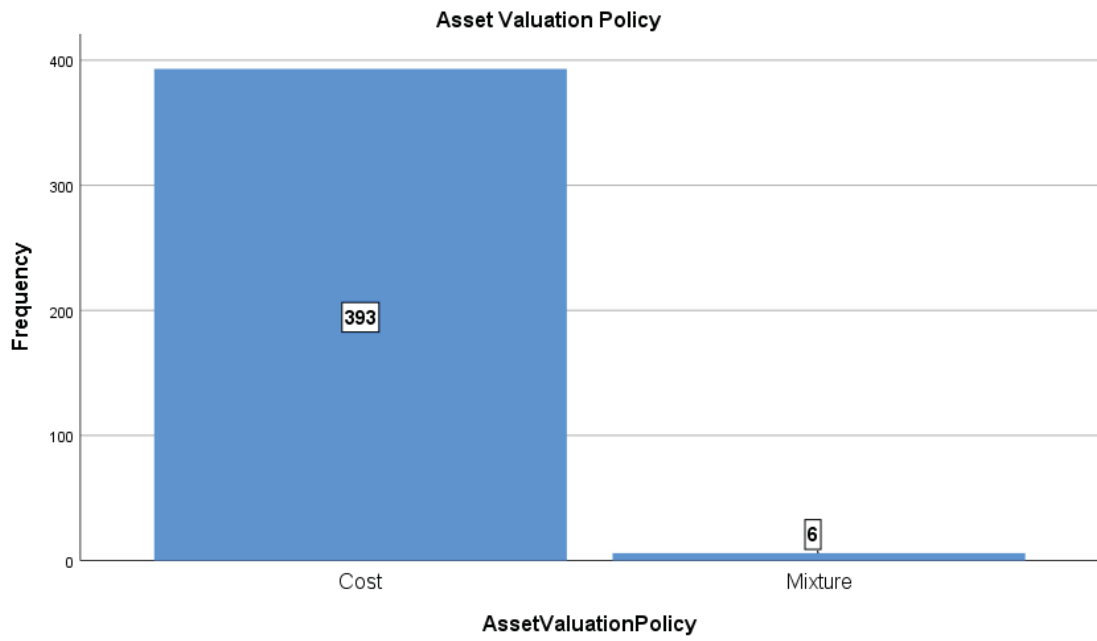
Figure A4.9 - Distribution of observations of the Asset Valuation Policy variable.
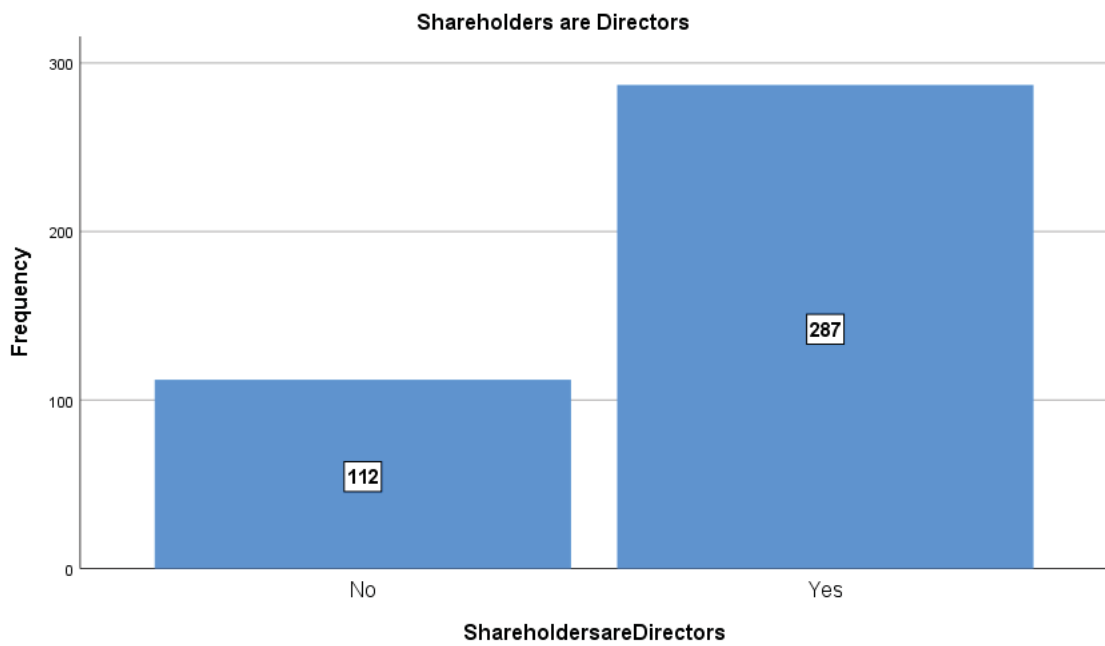
Figure A4.10 - Distribution of observations of the Shareholders are Directors variable.

A-24
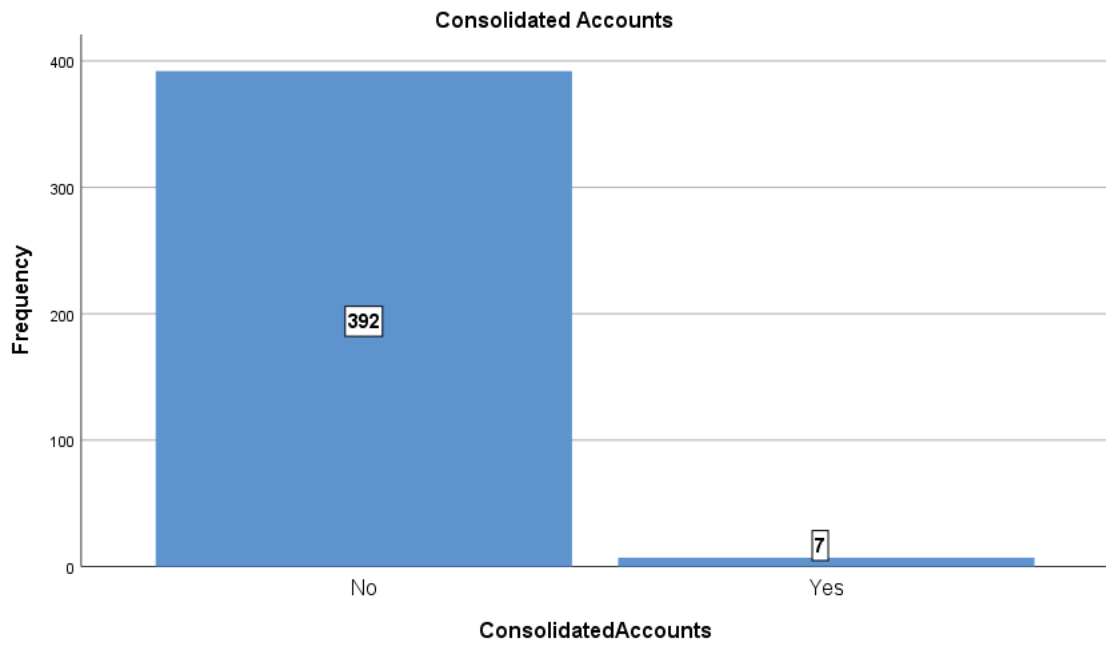
Figure A4.11 - Distribution of observations of the Consolidated Accounts variable.
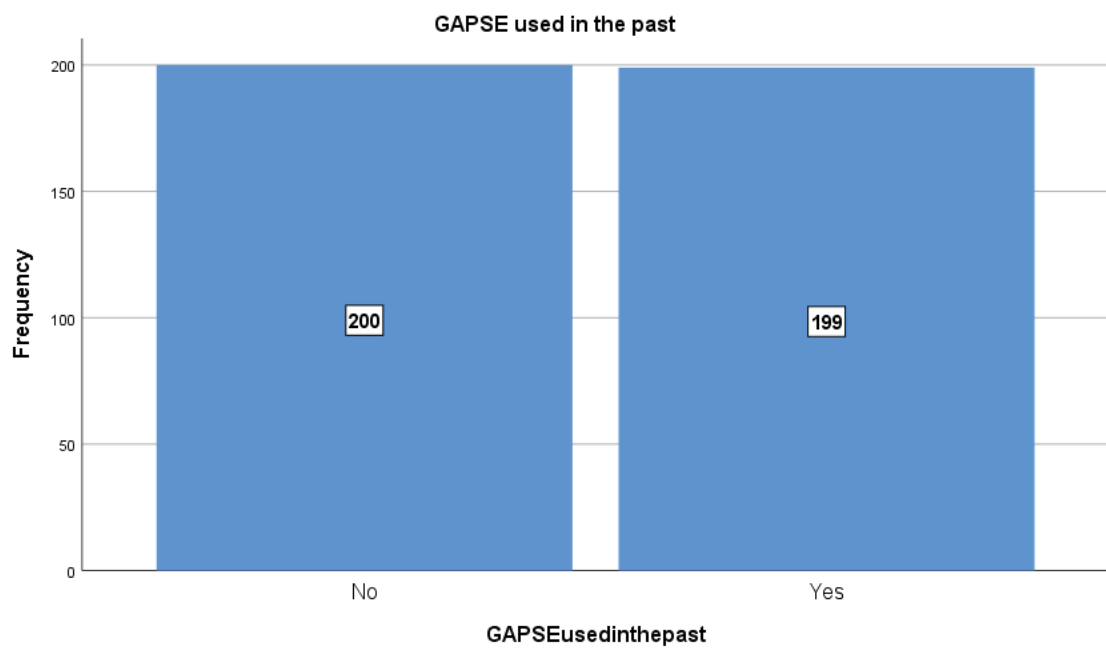
Figure A4.12 - Distribution of observations of the GAPSE used in the past variable.

A-25
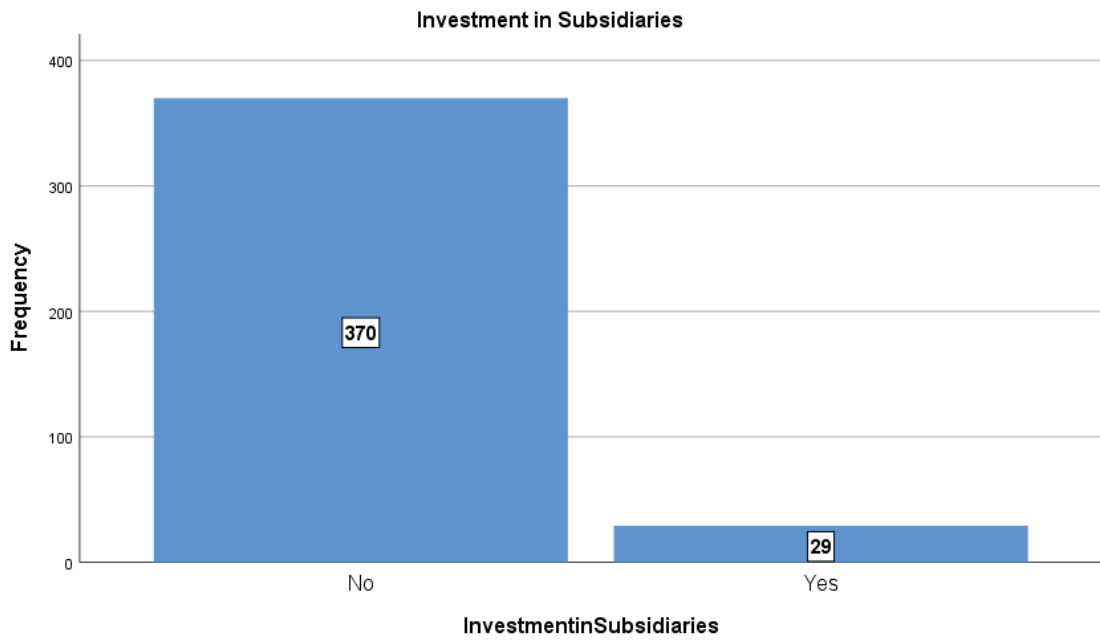
Figure A4.13 - Distribution of observations of the Investment in Subsidiaries variable.
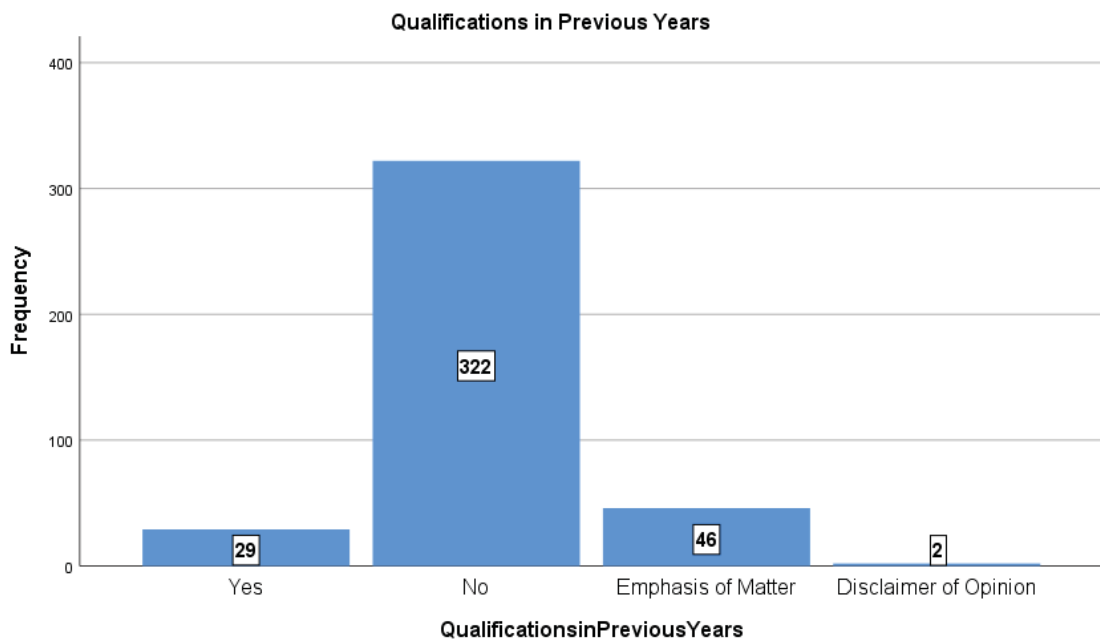
Figure A4.14 - Distribution of observations of the Qualifications in previous years variable.

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A4.2 – GOODNESS OF FIT INDICATORS

Model Summary

Step	-2 Log likelihood	Cox & Snell R Square	Nagelkerke R Square
1	231.272[a]	.331	.529
12	272.366[b]	.258	.413

a. Estimation terminated at iteration number 20 because maximum iterations has been reached. Final solution cannot be found.

b. Estimation terminated at iteration number 6 because parameter estimates changed by less than .001.

Table A4.3 - Model summary of the parsimonious model including the Nagelkerke R Square value.

Hosmer and Lemeshow Test

Step	Chi-square	df	Sig.
1	12.346	8	.136
12	7.679	8	.465

Table A4.4 - Hosmer and Lemeshow Test of the parsimonious model.

Classification Table[a]

			Predicted		
			UseofGAPSME		Percentage Correct
Observed			No	Yes	
Step 1	UseofGAPSME	No	44	33	57.1
		Yes	7	315	97.8
	Overall Percentage				90.0
Step 12	UseofGAPSME	No	31	46	40.3
		Yes	5	317	98.4
	Overall Percentage				87.2

a. The cut value is .500

Table A4.5 - Classification Table showing the overall percentage of correctness of the parsimonious model.

A4.3 – CHI-SQUARE TEST OF INDEPENDENCE RESULTS

A4.3.1 - Use of GAPSME Vs Size of Company

Crosstab

			Size		Total
			Small	Medium	
UseofGAPSME	No	Count	67	10	77
		% within UseofGAPSME	87.0%	13.0%	100.0%
		% within Size	17.3%	83.3%	19.3%
		Adjusted Residual	-5.7	5.7	
	Yes	Count	320	2	322
		% within UseofGAPSME	99.4%	0.6%	100.0%
		% within Size	82.7%	16.7%	80.7%
		Adjusted Residual	5.7	-5.7	
Total		Count	387	12	399
		% within UseofGAPSME	97.0%	3.0%	100.0%
		% within Size	100.0%	100.0%	100.0%

Table A4.6 – Cross-tabulation showing the association between the Use of GAPSME and Size of Company. (($\chi^2(1)$ = 32.575, p<0.0005, Cramer's V = 0.286)

Chi-Square Tests

	Value	df	Asymptotic Significance (2-sided)	Exact Sig. (2-sided)	Exact Sig. (1-sided)
Pearson Chi-Square	32.575[a]	1	.000		
Continuity Correction[b]	28.473	1	.000		
Likelihood Ratio	23.954	1	.000		
Fisher's Exact Test				.000	.000
Linear-by-Linear Association	32.493	1	.000		
N of Valid Cases	399				

a. 1 cells (25.0%) have expected count less than 5. The minimum expected count is 2.32.

b. Computed only for a 2x2 table

Table A4.7 - Chi-Square test results for Use of GAPSME vs Size of Company.

Symmetric Measures

		Value	Approximate Significance
Nominal by Nominal	Phi	-.286	.000
	Cramer's V	.286	.000
N of Valid Cases		399	

Table A4.8 - Symmetric measures table including Cramer's V value for Use of GAPSME vs Size of Company.

A4.3.2 - Use of GAPSME Vs Auditor Size

Crosstab

			AuditorSize				
			Big 4	Mid Tier	SMP	Sole Practitioner	Total
UseofGAPSME	No	Count	17	13	24	23	77
		% within UseofGAPSME	22.1%	16.9%	31.2%	29.9%	100.0%
		% within AuditorSize	42.5%	34.2%	17.4%	12.6%	19.3%
		Adjusted Residual	3.9	2.4	-.7	-3.1	
	Yes	Count	23	25	114	160	322
		% within UseofGAPSME	7.1%	7.8%	35.4%	49.7%	100.0%
		% within AuditorSize	57.5%	65.8%	82.6%	87.4%	80.7%
		Adjusted Residual	-3.9	-2.4	.7	3.1	
Total		Count	40	38	138	183	399
		% within UseofGAPSME	10.0%	9.5%	34.6%	45.9%	100.0%
		% within AuditorSize	100.0%	100.0%	100.0%	100.0%	100.0%

Table A4.9 – Cross-tabulation showing the association between the Use of GAPSME and Auditor Size. ($\chi^2(3) = 24.896$, p<0.0005, Cramer's V = 0.250)

Chi-Square Tests

	Value	df	Asymptotic Significance (2-sided)
Pearson Chi-Square	24.896[a]	3	.000
Likelihood Ratio	22.156	3	.000
Linear-by-Linear Association	23.092	1	.000
N of Valid Cases	399		

a. 0 cells (0.0%) have expected count less than 5. The minimum expected count is 7.33.

Table A4.10 - Chi-Square test results for Use of GAPSME vs Auditor Size.

Symmetric Measures

		Value	Approximate Significance
Nominal by Nominal	Phi	.250	.000
	Cramer's V	.250	.000
N of Valid Cases		399	

Table A4.11 - Symmetric measures table including Cramer's V value for Use of GAPSME vs Auditor Size.

A4.3.3 - Company Size Vs Consolidated Accounts

Crosstab

| | | | ConsolidatedAccounts | | |
			No	Yes	Total
Size	Small	Count	382	5	387
		% within Size	98.7%	1.3%	100.0%
		% within ConsolidatedAccounts	97.4%	71.4%	97.0%
		Adjusted Residual	4.0	-4.0	
	Medium	Count	10	2	12
		% within Size	83.3%	16.7%	100.0%
		% within ConsolidatedAccounts	2.6%	28.6%	3.0%
		Adjusted Residual	-4.0	4.0	
Total		Count	392	7	399
		% within Size	98.2%	1.8%	100.0%
		% within ConsolidatedAccounts	100.0%	100.0%	100.0%

Table A4.12 – Cross-tabulation showing the association between the Company Size and Consolidated Accounts. ($\chi^2(1)$ = 15.962, p<0.0005, Cramer's V = 0.200)

Chi-Square Tests

	Value	df	Asymptotic Significance (2-sided)	Exact Sig. (2-sided)	Exact Sig. (1-sided)
Pearson Chi-Square	15.962[a]	1	.000		
Continuity Correction[b]	8.288	1	.004		
Likelihood Ratio	6.241	1	.012		
Fisher's Exact Test				.016	.016
Linear-by-Linear Association	15.922	1	.000		
N of Valid Cases	399				

a. 1 cells (25.0%) have expected count less than 5. The minimum expected count is .21.

b. Computed only for a 2x2 table

Table A4.13 - Chi-Square test results for Company Size vs Consolidated Accounts.

A-31

Symmetric Measures

		Value	Approximate Significance
Nominal by Nominal	Phi	.200	.000
	Cramer's V	.200	.000
N of Valid Cases		399	

Table A4.14 - Symmetric measures table including Cramer's V value for Company Size vs Consolidated Accounts.

A4.3.4 - Auditor Size Vs GAPSE Use in The Past

Crosstab

			GAPSEusedinthepast No	GAPSEusedinthepast Yes	Total
AuditorSize	Big 4	Count	31	9	40
		% within AuditorSize	77.5%	22.5%	100.0%
		% within GAPSEusedinthepast	15.5%	4.5%	10.0%
		Adjusted Residual	3.7	-3.7	
	Mid Tier	Count	29	9	38
		% within AuditorSize	76.3%	23.7%	100.0%
		% within GAPSEusedinthepast	14.5%	4.5%	9.5%
		Adjusted Residual	3.4	-3.4	
	SMP	Count	47	91	138
		% within AuditorSize	34.1%	65.9%	100.0%
		% within GAPSEusedinthepast	23.5%	45.7%	34.6%
		Adjusted Residual	-4.7	4.7	
	Sole Practitioner	Count	93	90	183
		% within AuditorSize	50.8%	49.2%	100.0%
		% within GAPSEusedinthepast	46.5%	45.2%	45.9%
		Adjusted Residual	.3	-.3	
Total		Count	200	199	399
		% within AuditorSize	50.1%	49.9%	100.0%
		% within GAPSEusedinthepast	100.0%	100.0%	100.0%

Table A4.15 – Cross-tabulation showing the association between the Auditor Size and GAPSE use in the past. ($\chi^2(3)$ = 36.702, p<0.0005, Cramer's V = 0.133)

Chi-Square Tests

	Value	df	Asymptotic Significance (2-sided)
Pearson Chi-Square	36.702[a]	3	.000
Likelihood Ratio	38.198	3	.000
Linear-by-Linear Association	10.074	1	.002
N of Valid Cases	399		

a. 0 cells (0.0%) have expected count less than 5. The minimum expected count is 18.95.

Table A4.16 - Chi-Square test results for Auditor Size vs GAPSE use in the past.

Symmetric Measures

		Value	Approximate Significance
Nominal by Nominal	Phi	.133	.008
	Cramer's V	.133	.008
N of Valid Cases		399	

Table A4.17 - Symmetric measures table including Cramer's V value for Auditor Size vs GAPSE use in the past.

A4.4 – MANN-WHITNEY TEST RESULTS

A4.4.1- Audit Report Lag Vs Use of GAPSME
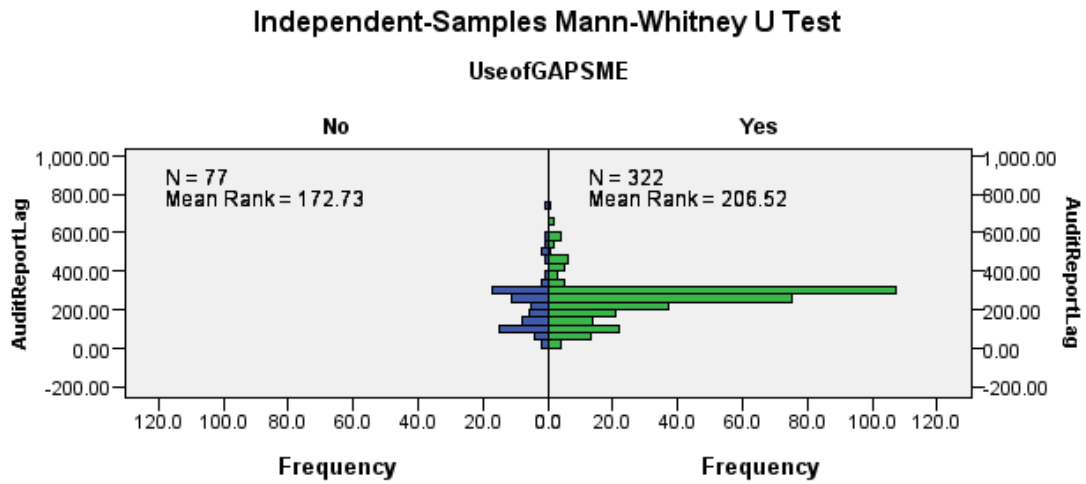
Total N	399
Mann-Whitney U	14,497.000
Wilcoxon W	66,500.000
Test Statistic	14,497.000
Standard Error	907.335
Standardized Test Statistic	2.314
Asymptotic Sig. (2-sided test)	.021

Table A4.18 - Mann-Whitney Test output for Auditor report lag vs Use of GAPSME.

A6 - INTERVIEW SCHEDULE – AUDITORS

1. What percentage of your clients do you think are SMEs, in terms of a range in percentages?

2. Do you believe that differential reporting for smaller entities is beneficial?

3. How do you see the GAPSME take-up when compared to the GAPSE take-up? Give reasons why in your opinion there might be a disparity between the two? What were the flaws of GAPSE that lead to the majority of SMEs in Malta adopting IFRS?

4. Do you consider GAPSME to be an inferior framework when compared to IFRSs as adopted by the EU?

5. When a company uses GAPSME, do you consider that company's audit risk is higher than if it were using IFRSs as adopted by the EU?

6. In practice, who makes the decision whether to use GAPSME or IFRSs as adopted by the EU?

7. In your opinion, what are the main drawbacks of GAPSME?

8. In your opinion, how have the changes introduced through GAPSME affected the different groups of stakeholders?

- Owners, shareholders and potential shareholders;
- Bankers and loan providers;
- Creditors;
- Accountancy profession

9. With hindsight, do you think GAPSME was issued at the opportune time considering the issued complex standards such as IFRS 5 - Non-current Assets Held for Sale and Discontinued Operations, IFRS 16 – Leases, IFRS 15 – Revenue from contracts with customers and IFRS 9 – Financial Instruments?

10. If GAPSME is meant to be a simpler version of IFRSs, did this lead to lower audit effort and subsequently lower audit fees being charged?

11. Did you observe any of the following cases:

- A company had opted for use of GAPSME in 2016 but reverted back to using IFRSs as adopted by the EU;
- A company which had adopted GAPSE in the past but did not adopt GAPSME;
- A company which is eligible to use GAPSME but has not adopted it, and if yes, what were the reason that caused such a decision

A7 - INTERVIEW SCHEDULE – SMEs

1. What were the factors which led your company to start preparing financial statements in accordance to GAPSME? If you used GAPSE beforehand, was it a considered to be the natural choice?

2. If the company also adopted GAPSE before, could you highlight the main differences, if any, between the two frameworks?

3. Who suggested the company adopts GAPSME?

4. What GAPSME simplifications have impacted the company most and which do you consider to be most beneficial?

5. Did the company incur any transitional costs directly related to the switch of financial reporting framework, and if yes, were such costs material?

6. If you answered yes to question 5, how long do you expect it will take to recover such transitional costs and these being translated into a cost saving?

7. What are your thoughts on the GAPSME recognition and measurement principles, and do consider them easier to follow those of IFRSs as adopted by the EU?

8. Do you consider GAPSME financial statements easier to prepare and has the simplified framework met your expectations?

9. Do you think the company may experience any other benefits through the use of GAPSME in the near future, which may not yet materialised?

10. How important is a financial reporting framework for the company? Would you still adhere to a financial reporting framework if this was not compulsory?

11. Did adopting GAPSME directly affect the cost of the company's audit?

12. Did banks accept the information provided through GAPSME financial statements, or did they often require supplementary information in order to achieve the same level of information provided IFRSs as adopted by the EU?

A8 - OFFICIAL LETTER OF INVITATION

L-Università
ta' Malta

Faculty of Economics,
Management &
Accountancy

University of Malta
Msida MSD 2080, Malta

Tel: +356 2340 2720

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DEPARTMENT OF ACCOUNTANCY
LETTER OF INTRODUCTION AND INVITATION TO PARTICIPATE IN RESEARCH

20/03/18

Dear Sir / Madam,

This is to introduce Matthew Sciriha, a Master in Accountancy student at the Faculty of Economics, Management and Accountancy at the University of Malta.

The student is undertaking research within the Department of Accountancy regarding the implementation and taking up of the GAPSME accounting framework in the Maltese scenario. This research aims to explore the extent to which GAPSME has been taken up by eligible firms, the reasons behind opting for GAPSME and possible reasons why one would still opt to use full IFRSs. Any correlation between variables such as the size of the firm in question, the meeting of small and medium thresholds, international trading and industry factors will also be looked into to try and establish relationships of possible causality.

In this regard, the said student would like to invite you to contribute on this research project by participating in an interview related to the study above and filling in a short questionnaire at your convenience.

This research is important and valuable in enhancing understanding of the subject area and helping practicing professionals and practitioners like yourself, as well as informing policy and support initiatives. The student would be happy to share with you general findings ensuing from this research.

The student is to ensure that any information provided will be treated in confidence, also in line with general Faculty research requirements and ethical obligations. A consent form will be separately provided. You are, of course, entirely free to discontinue your participation at any time or to decline to answer particular questions.

While I thank you beforehand for your consideration as well as your possible kind support and involvement in this important research, should you have any queries on this research please feel free to contact me via email at: accountancy.fema@um.edu.mt.

Yours sincerely,

Mr. Peter J Baldacchino
Head, Department of Accountancy
Faculty of Economics, Management and Accountancy

A9 - INVITATION E-MAIL SENT TO AUDITOR INTERVIEWEES

Dear _____ ,

Hope this email finds you well.

This email is addressed to whoever in the audit firm is most knowledgeable or deals with SME account preparation/auditing.

My name is Matthew Sciriha and I am sending this email as a request for your participation and support in my dissertation. You have been selected from a random sample to take part in my thesis titled, 'The implementation of GAPSME by Maltese companies – An Analysis' which partly fulfils my Masters in Accountancy course, which I am currently reading.

You are invited to take part in a 30 minute semi-structured interview relating to the GAPSME framework in Malta. All participants and responses will remain anonymous. Any information, opinion and collaboration towards the success of this study would be greatly appreciated.

Attached please find an official letter of invitation signed by the Head of Department of Accountancy, Faculty of Economics, Management and Accountancy at the University of Malta verifying the legitimacy of this study and this invitation for participation.

As one can clearly notice, the answers do not require any detailed technical knowledge on GAPSME but mainly opinion and feedback from your experience dealing with SME financial statements.

A reply with confirmation of your willingness participation would be greatly appreciated. Feel free to decline such an invitation if you do not wish to take part in the proposed study or send any concerns you might wish to address.

You will be briefed further before the interview and given an information sheet with all necessary information, together with a consent form which you will be asked to sign on your own accord.

Kind Regards,

Matthew Sciriha
Second year student, Masters in Accountancy, University of Malta.

A10 – INVITATION E-MAIL SENT TO SME INTERVIEWEES

Dear _____,

Hope this email finds you well.

This email is addressed to whoever in the audit firm is most knowledgeable or deals with SME account preparation/auditing.

My name is Matthew Sciriha and I am sending this email as a request for your participation and support in my dissertation. You have been selected from a random sample to take part in my thesis titled, 'The implementation of GAPSME by Maltese companies – An Analysis' which partly fulfils my Masters in Accountancy course, which I am currently reading.

You are invited to take part in a 30 minute semi-structured interview relating to the GAPSME framework in Malta. All participants and responses will remain anonymous. Any information, opinion and collaboration towards the success of this study would be greatly appreciated.

Attached please find an official letter of invitation signed by the Head of Department of Accountancy, Faculty of Economics, Management and Accountancy at the University of Malta verifying the legitimacy of this study and this invitation for participation.

If you could kindly reply as soon as possible with a confirmation of your willing participation in such a study, together with a time when I could come to the office next week and carry out the interviews.

As one can clearly notice, the answers do not require any detailed technical knowledge on GAPSME but mainly opinion and feedback from your experience dealing with SME financial statements.

A reply with confirmation of your willingness participation would be greatly appreciated. Feel free to decline such an invitation if you do not wish to take part in the proposed study or send any concerns you might wish to address.

You will be briefed further before the interview and given an information sheet with all necessary information, together with a consent form which you will be asked to sign on your own accord.

Kind Regards,

Matthew Sciriha
Second year student, Masters in Accountancy, University of Malta.

A11 – WORD COUNT EXTENSION

EXTENSION OF WORDCOUNT LIMIT

Date: 9th May 2019

I am hereby requesting a word extension from 15,000 words to 20,000 words as a limit for my dissertation titled, "The Implementation of GAPSME by Maltese Companies - An Analysis", in order to allow for a more comprehensive discussion of the findings obtained.

The signatures below provide evidence of the granted authorisation with regards to the word extension.

Mr. Frank Cassar

Dissertation Supervisor

Matthew Sciriha

Student

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