

# The system about accounting transparency and the introduction of the accounting standards for unlisted small and medium sized companies

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## 〈Abstract〉

The purpose of this study is to research systems about accounting transparency and to present how to introduce the standards in accounting unlisted small and medium sized companies. In Korea, the measures of enhancing accounting transparency of enterprises was mainly focused on the listed enterprises. On the contrary, the measures on enhancing accounting transparency of the SMEs was relatively insufficient

This study researches systems regarding accounting transparency in Korea and reviews the previous studies about the accounting transparency in small and medium-sized companies. This study also research other countries' accounting standards specialized only in the unlisted small and medium sized companies in order to establish accounting standards in the unlisted small and medium sized companies in Korean

For the new accounting standards for SMEs, this study suggests both strengthening part and alleviating one, comparing to the current enterprise accounting standards. Each has three points to discuss. For the alleviating part, those standards should be simple, understandable and fit to the incumbent tax law. For the enforcement part, those standards should stand with the accounting reality of the small and medium sized companies, and it should also contain detailed expressions of the accounting transparency and managerial accounting.

Key word : accounting transparency, the accounting standard, the special standard of accounting of unlisted small and medium sized companies

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## I . Introduction

Korean economic situation has suffered from the low level of growth and the high level of unemployment due to the economic crisis in 2008. It is important to invigorate the national economy and stabilize employment to overcome such crisis. Thus, it is necessary to secure investment and support for the small and medium sized enterprises('SME' below) in order to strengthen the national economy and make sure of stable employment. To promote investing and support the SMEs, it is prerequisite to secure accounting transparency. However, in reality, the accounting transparency of the SMEs is generally very low. So far, the government has made efforts to secure accounting transparency by introducing international financial reporting standards. This has been focused on the large enterprises. Therefore, it is necessary to take measures for securing accounting transparency for the SMEs.

The accounting transparency is a level of providing important information for the accounting information users. Kim et al.(2006) stated that the accounting transparency means a state that the accounting information is transferred under the environment where the process and the contents of the information are sufficiently open to the information users so that there is no room for doubt. Elliott et al(2009) said that accounting transparency is to minimize uncertainty of financial profit i.e. minimizing gap between the profit on the financial sheet and the real profit.

The problem of accounting transparency of a company is a fundamental basis of the capitalism. The government designated 2001 as a year of eradicating accounting fraud and made a lot of efforts to enhance transparency of corporate finance after undergoing 1997 currency crisis and 2001 Enron collapse. Facing Financial crisis in 2008 aroused the importance of moral transparency of enterprises. In 2006, the government gave listed enterprises additional chance of self revision in spite of nationwide opposition, which was a part of efforts intending to achieve accounting transparency of the listed enterprises.

In Korea, The measures of enhancing accounting transparency of enterprises was mainly focused on the listed enterprises. On the contrary, the measures on enhancing accounting transparency of the SMEs was relatively insufficient. The proportion of the SMEs in the nation-wide economy is very large. Thus, the poor accounting transparency of the SMEs will affect those of the large enterprises, which mean the accounting transparency of the SMEs has a significant effect on the market as a whole.

This study is, first, to look into institutions for securing accounting transparency. Also, it will look into the possible measures to introduce accounting standards that are easy to use and take less expenses. It is necessary to introduce standards that secure accounting transparency without taking much expenses. For sure, the SMEs have to make their own efforts but the institutional supports are also very important. Recently Korea federation of small and medium business(KBIZ) also suggests the importance of the accounting standards for the SMEs.

This study was intended to suggest urgent needs to introduce the accounting standards for the SMEs' finance that will be covered in a way minimizing financial burden on the SMEs and maximizing its usability. It is necessary to introduce new institutions securing accounting transparency without great expenses. The SMEs need to make their own efforts but the more important thing is that the institutional systems should be revised to support them. KBIZ also suggests the needs for the accounting standards for the SMEs

The followings are needs for the study on accounting transparency for the SMEs. First, under the situation that K-IFRS is getting difficult and a cut on external audit subjects, it is getting more important to introduce new institutions to secure accounting transparency of the SMEs. Secondly, the accounting transparency of the SMEs affects those of large ones and similar ones in a chain one by one. That is to say, trades without proof of the SMEs can affect the trade-related companies in many ways. Heo(2004) pointed out that the SMEs are stading on the fundamental positions in our national economic hierarchy. Thirdly, reinforcement of transparency of the SMEs will encourage business people to invest in the SMEs. Fourthly, it is needed to find management plans for a company to secure accounting

transparency. Fifthly, there are growing requirements for a company to take social responsibilities. Accounting transparency is important to secure reliability which is closely related to national fame(Park, 2002). There is increasing pressure for the companies to have accounting transparency as a first step of taking social responsibilities.

The purpose of this paper is like below.

First, this is to call an urgent need for setting up the financial reporting standards for the SMEs, covering related institutions. In the pre-study, accounting transparency related institutions were covered in order to suggest needs for setting up the financial reporting standards for the SMEs.

Secondly, concrete plans about financial reporting standards for the SMEs are suggested. In following chapter, you will see how to improve usability of a balance sheet by introducing financial reporting standards. It will naturally contribute to enhancing accounting transparency of the SMEs.

The utility of this paper is like below.

First, this paper starts discussing the reason why it is important to introduce independent and different SME financial reporting standards. The necessity of such standards will be prompted by reviewing contents of related institutions and studies covered in the pre-study.

Secondly, this study will contribute to enhancing reliability of financial information of the SMEs. In a current setting, it is hard for small or medium companies to know if their balance sheets are made properly or not. Thus, It will enhance reliability of financial information of the SMEs if a person in charge of making its own balance sheet with understanding of the standards.

Thirdly, enhanced transparency will encourage investment and support for the SMEs. It will also help efficiently distribute limited resources from the government. Financial institutions, investors, and the government can utilize the financial information about the SMEs and it will help them distribute their own resources for support efficiently.

Fourthly, this study can give meaningful information about management efficiency of the SMEs, giving the managers useful information which they can use to make better decisions. Therefore, the SMEs can use these sets of information in making their plans by using them according to their own accounts.

This study will deal with its background, necessity, purpose and usability in the chapter 1. In the chapter 2, the pre-study is reviewed. The pre-study mainly deals with the measures and institutions introduced to secure accounting transparency of the SMEs. The chapter 3 contains foreign examples and possible measures to introduce independent financial reporting standards for the SMEs, Lastly, the chapter 4 gives conclusion and limits of this study.

## **II. The pre-study on the measures to secure accounting transparency of the SMEs.**

### **1. Pre-study**

The measures already taken are reviewed and the results of the pre-study will be reviewed.

#### 1.1 The measures already taken.

##### 1.1.1 Foundation of KAI

Foundation of Korea Accounting Institute(KAI) is a major example of the measures already taken. KAI is founded in September, 1999 to perform tasks related to financial reporting standards. It is to keep integrity and objectiveness of corporate finance and external audit. It's been dealing with legislation, revision, interpretation of financial reporting standards and other related works according to the law on the external audit of the Corporations. It also has Korea Accounting Standards Board(KASB), a subsidiary agency consisting of related experts to take audit and decide on the standards. It published K-IRFS in the end of 2007. Since 2011, every listed companies have to go public, applying K-IRFS. It made Korea acknowledged as a country acting on the IFRS.

##### 1.1.2 Enforcement of financial authorities' supervision and financial inspection

Financial authorities' supervision has been reinforced. According to Kim

and Shim(2004), The financial authorities have been reinforcing the inspection on finance of domestic enterprises in order to enhance accounting transparency and reduce accounting scandals but still it has to be reinforced even more. Recently, Financial Supervisory Service(FSS) has expanded the number of its audit subjects, resulting in proportion of inspection result indications. Accordingly, it naturally increases the number of sanctions on the inspectors such as a certified public accountants or financial corporations.

In November, 2011, the Securities and Futures Commission(SFC) published “measures of accounting internationalization.” It limits companies to take financial audit only by the registered accounting firms. Moreover, It prohibits the submitted financial balance sheet from editing. Previously, the balance sheet was easy to be modified during the audit both by the accountant or the audit subject. Thus, as of now, the settlement of financial balance sheet should be submitted to the SFC so that it can be audited in depth. On the other hand, external auditors will be nominated among external executives by audit committee independent from the internal management.

### 1.1.3 Introduction of institutions to enhance corporate governance

In order to enhance accounting transparency, concentrated voting and external executives were introduced. Ever since IMF, the corporate governance has been a problem and the social pressure to revise it has been growing gradually. There are several examples of revising it by institutional devices. The major ones are concentrated voting to protect minorities and external executives.

Such institutions can prevent the largest shareholder from taking all the control, protect minority and supervise the management so that the managerial transparency can be secured.

The external executive system was introduced first in February 1998 with revision of “regulation on securities listing” and in 2001 introduced in the law on securities trading. According to these institutions, companies have been designating professors, public officials or executives from the other companies as their external executives. Finance Supervisory Service gave

external executives the right to ask information in order to enhance transparency of the company, The external executive system gave a result of modifying election of executives and its function of 2 of 3 major agencies(general meeting of shareholders, inspection, board of directors) of a company. Especially, the board of directors which dealt with mainly internal issues has been completely transformed into an external inspection agency. Jeon and Lee(2011) pointed out that the higher proportion of external executives in the board of directors is, the higher ROA is guaranteed

#### 1.1.4 Obliging of building internal control structure.

The article 28 of the law on the capital market and financial investment and its ordinance article 31 obliges companies to have internal control system. The internal control system has become obligatory for the inspection subjects according to the law on the external audits of the Corporations. According to the desirable internal accounting management standards, the internal control system is a set of process to achieve compliance to relevant laws and policies(compliance purpose), reliability of financial information(financial reporting purpose), and efficiency and effectiveness of management(operational purpose). Such processes are constantly performed by the board of directors, management, and other members of a company. That is to say, the internal control system is to diagnose and evaluate if the essential work processes are performed well according to the internal control standards. Kim and Park(2002) emphasized the importance of improving the internal control systems in order to secure accounting transparency. Yu and Park(2011) pointed out the improvement of the internal control systems is very important not only in respect to financial aspect but also in respect to taxation aspect. Doyle, et al.(2005) wrote that the internal control systems should be strengthened especially for the rapidly growing companies. The internal control systems have been constantly strengthened as the standards of internal audit in the law on the external audit of the Corporation also has been strengthened.

#### 1.1.5 Introduction of K-IFRS

The government announced the roadmap on the international financial

reporting standards decided by the international accounting standards committee. KASB announced 'Bound Volume' consisting of 37 revised K-IFRSs adopted by Korea, 25 interpretations and concepts of writing and indicating financial sheets.

The finance sheets of every listed enterprises have been obligatory to be made according to K-IFRS since 2011.

#### 1.1.6 Introduction of compliance officers

The article 54-13 of the commercial law prescribes listed companies under the President decree to be prepared with compliance control standards to comply with the law and manage the company according to the law. To do so, the pertinent companies should nominate more than one compliance officer.

In the case of financial institutions, the compliance officers work full time. Meanwhile, the listed companies don't have such compliance officers so that they have been criticized that they don't keep up with the international trend of moral management. Thus, the commercial law was revised since moral management and social responsibility of the companies became more important.

#### 1.1.7 Summary

Most of the institutions about accounting transparency are for the listed enterprises. The listed enterprises have more chances of window dressing settlement, international trades, donating all the trades to a subsidiary and even using the SMEs to do window dressing settlement. Therefore, the question of accounting transparency is required not only for the listed enterprises but also for the SMEs.

In this social ambient, the accounting transparency of the SMEs gets important more over more. In fact, the SMEs take more proportion in the national economy which gives them more responsibility than the listed enterprises. However, the SMEs generally have the weaker inspection functions than the listed enterprises and the measures to secure accounting transparency are focused on the cases of the listed enterprises.

Moreover, the SMEs are having more issues that make the accounting transparency much more important. These issues are the extension of the union, increase of management participation by employees and social responsibility issues aroused by the multi-national companies of the foreign countries. In spite of these management conditions, the national SMEs lack accounting personnel and weak at international responses.<sup>1)</sup>

## 1.2 Study on securing accounting transparency of the SMEs.

The pre-study on the measures to secure accounting transparency of the SMEs is like below.

### 1.2.1 Enhancement of the perception on the moral consciousness and accounting

Kim(2004) stated that collection of accounting information of the non-audit subjects and writing a financial sheet of a SME are focused on avoiding taxes, acceptance of governmental orders, and taking loan from financial agencies. Due to the lack of social awareness of accounting transparency, people in charge of finance tend to decide on relevant matters according to their experiences or intuition. Therefore, CEOs of non-audit subjects(among the SMEs) need to focus on the moral consciousness of the companies in order to maintain accounting transparency. Moreover, the companies should be aware of the fact that accounting takes a significant part in management and emphasize on utilizing accounting information in making decisions and measuring performance of the companies.

Furthermore, VAT ratio and Corporation tax ratio should be reduced in order to encourage the companies to pay tax properly so that accounting transparency should be naturally increased.

### 1.2.2 Obliging regular accounting education.

Kim(2004) stated that those who are in the charge of accounting in the non-audit subjects or the CEOs of such companies may lack professional knowledge on accounting, which leads such companies lack accounting

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1) KBIZ(2019. 9. 19) announced that 60% of the corporate of the equity size below 50bil won has thlaccounting personnel and 40% of those with the equity size above 5 bil to 7bil has 1 accounting personnel.

transparency. In this case, it is useful to introduce regular education of accounting for such personnel to get professional knowledge for a certain periods. That is, those people should be educated in relevant accounting agencies such as KACPTA(Korean Association of Certified Public Tax Accountants), KICPA(Korean Institute of Certified Public Accountants), SMBA(the Small and Medium Industry Promotion Corporation), universities and etc. Kim et al.(2006) also pointed out that it is important to educate those in charge of accounting in the SMEs in agencies such as SMBA or KCCI(Korea Chamber of Commerce and Industry). The education should be executed regularly in order to reinforce its effectiveness. Thus, it is important to build an educational environments and effective educational programs and its range.

#### 1.2.3 Independent accounting standards for the SMEs.

Kim et al.(2006) stated that the independent accounting standards are needed since the current enterprise accounting standards are difficult. Hwang et al.(2009) pointed out that, given introduction of IFRS, the listed corporations should apply K-IFRS and the unlisted ones should apply independent standards simplified for the SMEs. Hwang et al.(2009) also stated that it is desirable to introduce accounting standards for the unlisted companies which is modified and simplified from existing accounting standards which are complicated for the SMEs. Shim(2007) suggests that the accounting standards should be classified by the size of the companies. IFRS is difficult for the SMEs to comply with even though it has exception laws for the SMEs. Shim(2007) also stated that overly strict accounting standards may deter the unlisted companies that are to willingly enhance accounting transparency. Thus, what Shim(2007) said was that the simplified accounting standards for the small enterprises that have employees under 5 people is needed.

#### 1.2.4. Strengthening preferential treatments for the listed corporations that receive voluntary external audit

Shim(2007) stated that the basic reason why the SMEs modify their profit

figure is that they perceive disclosing transparent accounting information as expense rather than benefit. The preferential treatments for those who take voluntary external audits will encourage the SMEs to go for the transparent disclosure of accounting information and willingly take the external audits. The external audits are surely expense for the SMEs. However, if negative perception of foreign investors and accordingly generated financial risks are exchanged into benefits for the SMEs taking voluntary external audit and if there are tax and interest incentives, it will promote accounting transparency of the SMEs. Currently, the government rewards the SMEs taking voluntary external audit by giving them higher credit rating but they don't take it as an advantages. Therefore, the efforts should be made to make more benefits for the SMEs and communicate those benefits with them. Kim et al.(2006) also stated that the government should aid a part of audit fee for the SMEs taking voluntary audit and give them audit exemption and interest advantages during the acceptance periods with advantage points when they apply for the policy fund.

#### 1.2.5. Sharing financial sheet for tax of the SMEs with the taxation authority

Shim(2007) stated that the SMEs lower their profit figure in order to reduce tax to pay but they raise the figure when submitting the financial sheet to the financial agencies in order to pay the debt at lower interest rates. Therefore, if the information user can use both reports, the SMEs become more careful to modify the figures. The taxation authority shows some movements to share the information only with agreement based on the article 81-1 of [the basic law on the national tax](condition of secrecy) and the article 10 of the law on protection of the use of personal information by the public institutions(the use of the processed information and limit of sharing). Still it is insufficient to have effectiveness. Thus, the taxation authority should perceive the tax information as public goods and share it with financial agencies and rating agencies.

#### 1.2.6. Building harmonized tax law with accounting system

Kim et al.(2006) stated that it is important for the SMEs to build

coordinated accounting system because the SMEs are the basis of taxation standards by fair taxation principles and back datas of the national macro statistics. Kim(2004) stated that the SMEs are having difficulties in calculating the profit of the given fiscal year due to the extremely complicate taxation process and frequent modifications of the law. If the non audit subjects can skip such complicated process and count the net profit during the fiscal year as their taxable income, it will simplify the process for the subjects and make the tax administration more efficient. The whole tax income is expected to be decreased but it won't affect the national finance. By this way, the accounting standards for the SMEs may get more consciousness and enhance accounting transparency.

#### 1.2.7 Building the national accounting intra-structure

Kim et al.(2006) stated that in the future, it is needed for the economic units should be prepared for the changed financial environments since there is negative image on the accounting transparency of the SMEs. It is also important to build an evaluation system to assess technical skills and prospect for development. Kim(2004) stated that if the SMEs have to submit the financial sheets inspected by external auditor in order to receive an order from the government or the local government, it will help the infra-structure be built.

Hwang et al.(2008) stated that the education at the universities is the starting point of eradicating the accounting fraud. In the universities, the students should learn how to expose accounting frauds. The education at the universities will be a great part in enhancing the accounting transparency.

Kim(2004) stated that regular moral education for the tax officers is also important because the tax officers are in the charge of the accounting process of the non-audit subjects. However, there are cases that even tax officers help the companies do the window dressing settlement both willingly or by request of the companies. Therefore, the tax officers should have proper works ethic and educated to be so. The education should be done by the accountants of the tax offices or KACPA. The accounting education should be done accordance with the accounting education by KAI or relevant

agencies on a regular basis.

#### 1.2.8 Reinforced management of the paper works of tax officers and accountants

Shim(2007) pointed out that the half of the companies outsource process of making financial sheets so that the tax officers and accountants are responsible for the accounting transparency of the SMEs. However the competition between tax officers and accountants made them to lean towards listening to the customers' requests. This tendency may be corrected by registering the tax officers who do frequently financial frauds on the Korean corporate data and share the list among the financial agencies. Kim(2004) stated that the efforts should be made to secure responsibility and morality of the tax officers and accountants.

## 2. The differences with the pre-sturdy

The pre-studies were focused on accounting transparency of the large corporates and the measures to secure it. There are no concrete measures to secure accounting transparency of the SMEs. In this process, the accounting standards for the companies, which are the basis of enhancing the accounting transparency, become more complicated for the SMEs to understand or comply with.

Therefore, in this study, the accounting standards for the SMEs, which is independent from the existing accounting standards, are suggested since they help the accounting transparency of the SMEs enhanced. The concrete measures which were not included in the pre-study will be suggested as below.

First, by simplifying the accounting standards for the SMEs compared to that of the large ones, the measures to secure accounting transparency for the SMEs will be suggested. That is to say, the standards have to be simplified so that the SMEs can understand and comply with the simplified standards by themselves. The measures should be consistent, easy to

understand and comply with.

Secondly, the articles regarding the SMEs should be reinforced. The articles regarding the SMEs should be specified and better defined. Plus, the SMEs should understand well about their profit figures. The index regarding the managerial index should be included in the standard so that the SMEs should better understand and utilize the financial information.

Thirdly, the measures to disseminate the new standards should be invented. The measures to disseminate the new independent standards will be suggested.

### **III. Introduction of the accounting standard for the SMEs**

#### **1. The pre-study on introducing the accounting standards for the SMEs.**

The 14 articles of the standards have 12 exceptional articles for the SMEs' accounting process. And only 57.3% of the SMEs apply 1~2 acts as of now. Especially, 22% of the SMEs never used the exceptional articles of the accounting standards.(Hwang et al., 2009) There are 7 exceptional parts relevant to the SMEs, evaluation by cost method of short-term securities, exemption of evaluation by equity method for equity security, evaluation of nominal value of long-term debt/bond, application of service life corporate tax, exemption of deferred corporate tax, omission of writing net profit per share and omission of writing information by business department. Two of them are related to the index of financial sheet. As a result of analyzing the current standards article 14; exception laws for the SMEs, deferred corporate tax, net profit per share and evaluation of the current value are frequently used while the other articles are not used. In the study of Choi and Hwang(2008), they suggest 3 level structures of enterprise accounting, the listed companies, the unlisted but audit subjects and non-audit subjects. There are other studies suggesting the needs for the accounting standards for the SMEs in order to enhance accounting

transparency of the SMEs; Kim et al.(2006) Study on accounting transparency of the SMEs, Kim(2004) Study on securing accounting transparency of the non-audit subjects, and Shim(2007) Study on securing accounting transparency of the non-listed SMEs.

## 2. Problem of the current enterprise accounting standards

The current enterprise accounting standards are focused on the large companies and has some exemptional articles for the SMEs in its chapter 31. In order to know the exemption articles, the companies should know the whole standard in depth, which makes it hard for the SMEs to be well aware of such exemptional articles. Therefore, it is necessary to find out accounting standards for the SMEs, which are easy to understand, in order to enhance accounting transparency of the SMEs. As shown in the <table 1>, proportion of the companies making self-accounting book keeping by themselves, ranging from its asset size 7bil won to 10bil won, is less than 50%.( 48.5%) It is very low proportion

In order to make accounting standards for the SMEs use the accounting standard more easily, the enterprise accounting standards have exemption laws. The purpose and range of such exemption laws are like below. “This standard is to alleviate accounting burden for the SMEs by deciding necessary parts for awareness, measurement and publication. The standard is applied to the SMEs’ accounting process under the law on the external audit of the Corporation. This standard can be used for the non-audit subjects as well.

<Table 1> The ways to keep accounts

Asset size(won)	Self-writing	Out sourcing	Both way	Total
Under 500mil	5.8	71.1	23.1	100
Above 500mil under 2000mil	8.9	70.1	21	100
Above 2000mil under 5000mil	22.2	51.9	25.9	100
Above 5000mil under 7000mil	37.1	40	22.9	100
Above 7000mil under 10,000mil	48.5	25.8	25.7	100
Above 10,000mil	79.1	7.4	13.5	100
Average	35.3	43.5	21.2	100

\* Survey by KBIZ(2011.09.19)

### 3. The needs for the accounting standards for the SMEs

As shown in the table 1, the SMEs usually don't spend much money on accounting. The table 2 shows the reasons why the SMEs are having difficulties using the accounting standards. The survey shows 57.5%(21.5%+36%) of the SMEs are experiencing difficulties using the accounting standards. 33.8% of the individuals responded that the current standards are too complicated to understand. 19.2% of the corporate responded that the enterprise accounting standards are very difficult. 37.5% of the corporate and 28.4% of the SMEs responded that there are too much articles to apply. These difficulties should be resolved by introducing the accounting standards for the SMEs.

<Table 2> difficulties of the current enterprise accounting standard<sup>2)</sup>

Difficulties	Corporate	Individuals	Total
a. Hard to understand	19.2	33.8	21.5
b. Too many articles to apply	37.5	28.4	36
c. Too much expense to manage	16	24.3	17.3
d. Different from the tax law	27.3	13.5	25.2

\* Survey by KBIZ(2011.09.19)

### 4. The foreign cases of the independent accounting standards for the SMEs.

China and America have the independent accounting standards for the SMEs.

China has the accounting standards for the small companies while America applies OCBOA(Other comprehensive basis of accounting) for the SMEs

2) KBIZ did the survey with the sample of 527 corporate and 100 individuals.(628 in total)

## 4.1 The accounting standards for the small companies in China

### 4.1.1 The accounting standards for the small companies

The Chinese ministry of finance announced “The accounting standards for the small companies” on 47, April, 2004 and implemented it on 1, January, 2005 in the nation as a whole in China. The standards is based on the law on finance of the People’s Republic of China<sup>3)</sup>

The accounting standards for the small companies are applied to the small sized companies established in China except the companies with public aspects and subsidiaries of the large companies.

The companies with public aspect means that the company has stocks or bonds traded on the market or the financial agencies(banks, insurance companies and other fund management companies). The small sized companies means that the companies categorized as small companies and micro companies according to the relevant law on SMEs.

The small companies under the accounting standards for the small companies can use the standards by their choice. The standard prescribes that the small companies can also use the corporate standards. However, once they choose to use the corporate standards, they can’t use the accounting standards for the small companies.

### 4.1.2 Differences from the normal accounting standards.

The study of 羅素清(2005) shows differences between the normal accounting standards and the accounting standards for the small companies as below.

First, there are reduced numbers of accounts. The normal accounting standards have 85 accounts in the first class while the standards for the small companies only have 60 accounts in the first class. For the second and third classes, the normal accounting standards have 74 accounts while the one for the small companies has 56 accounts.<sup>4)5)</sup>

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3) The small company is defined by its kind. the small and medium business is defined in [the law on the standard for the SMBs].Among them, those with relatively small sized companies are the small companies.In case of the manufacturer, the medium size means the company with employees above 300people, sales above 30mil won, the equity above 40mil, and the rest is defined as small companies

Secondly, imputed time related un-realized profit is treated as cash basis. Un-received financial interest or arbitrary debt is not counted.

Thirdly, rules regarding capitalization are simplified. Evaluated profit of the equity is not counted but the cost evaluation is applied. The current value of the financial lease is not counted. Depreciation of the long-term equity is ignored.

Fourthly, the report of settlement only needs the financial sheets and the statement of profit and loss. No Cash flow table or cost statements are required.

## 4.2 Accounting policies for the SMEs in America

### 4.2.1 The accounting policies for the SMEs

In America, there is no federal financial law or the corporate law but each states have its own corporate laws. The American accounting standards were developed from [the law on federal trade of securities]. The companies under [the law on federal trading of securities] have to make the financial sheets by GAAP prescribed b FASB. Moreover, the companies whose stocks or bonds are traded in the market should submit the financial sheets to SEC according to the law on trade of securities.

The un-listed companies don't have to make the financial sheets according to the federal law so that the creditor, shareholder can make the reports by the needs of the information users. SAS No. 62(The special report) states that the un-listed companies can make the report according to OCBOA.

FASB announces the general rules by the accounting principles. The

4) The samples of the first class accounts, the second accounts and third class accounts

一级科目	二级科目	三级科目
固定資産	生産用固定資産	生産用房屋
		生産用机器设备
應付账款	应付E单位账款	
	应付F公司账款	
庫存商品	甲商品	
	乙商品	

5) In the accounting standard for the small companies, the first level account sees the raw material and the package as one account(material) deprivation of the longterm asset, unfixed financial asset expense, un fixed asset profit and loss can be ommitted.In the accounts regarding the debt, unpaid dividend and arbitrary debt can be ommitted.

accounting process by GAAP provides the financial sheet with financial transparency. The SMEs have to spend much money to comply with GAAP. Thus, there are exemption rules for comprehensive accounting(Delaney 2009).

#### 4.2.2 Difference from the general accounting

The general accounting standards make the financial sheets based on the accrual basis. However, the unlisted companies can make the financial sheet based on OCBOA. There are three OCBOAs.

First, the billing is processed on receiving the cash on the cash basis, which generates no problem regarding the evaluation.

Second is the mixed method with revised cash basis and accrual basis. This is based on accrual basis but defer all the accounts except profit in advance or sales deposit.

Thirdly, tax law basis follows calculation of the Tax Return. Exclusion from gross income and Exclusion from gross loss should be reported in the index of the profit and loss statement. On the other hand, OCBOA doesn't require making of the cash flow table.

### 5. The method to introduce the accounting standards for the SMEs.

#### 5.1 The direction of introduction.

The accounting standards for the SMEs should have both strengthening and alleviating aspects, compared to the current accounting standards. The alleviating aspect includes making the standards easy to understand, easy to apply and consistent with the law. The strengthening part includes applying the current state of the SMEs, clarifying the standards regarding accounting transparency, strengthening the managerial accounting aspects. The essential parts the accounting standards for the SMEs should have are listed in the <table 3> below. The SMEs which are corporate sees "easy to understand" as the most important part(30.6%) while the SME which individuals sees "easy to apply" as the most important part(32.7%). The corporate sees "consistent with the tax law" as the second important part(27.3%). This is

partly because the tax required for the corporate is more complicated than that for the individuals. The individuals see “easy to apply” as the second important part(31.7%). The accounting professionals put more importance on “easy to apply”. Besides, the financial agencies regard “reflecting the current state of the SMEs” as the most important part(73.1%). This study utilizes the data gathered by KBIZ and suggests the method to introduce the accounting standard for the SMEs.

&lt;Table 3&gt; The direction of introduction

Contents	The SMEs			Accounting professionals		Financial agencies
	corporate	Private firms	total	CPA	CTA	
Easy to understand	17.8	32.7	20.2	10.7	13.4	6.1
Easy to apply	30.6	31.7	30.7	36.6	34.8	7.9
Reflecting the current state of the SMEs	24.3	24.7	24.4	34.4	18	73.7
Consistent with the tax law	27.3	10.9	24.7	17.2	33.2	11.4
Others	-	-	-	1.1	0.6	0.9
Total	100					

\* Survey by KBIZ(2011.09.19)

## 5.2 Alleviating aspect

### 5.2.1 Making the standards easier to understand

The current enterprise accounting standards are targeting the whole companies of various size so that the contents are enormous and complicated. The accounting standards for the SMEs affect restricted range of the companies so that it has to be made easy for the staffs to understand by using the frequently occurred cases.

The enterprise accounting standards should be composed based on the financial sheets. Therefore, counting and evaluation of the asset and debt on the book should take a lot of parts in the standards. However, the SMEs are more interested in the profits and losses for the current term rather than the financial state. Thus, for the SMEs, to well understand the information regarding profits and losses, inventories and securities should be under the

cost basis and the long-term asset or debt should be excluded from the value evaluation so that the evaluation of the asset and the period should be minimized in the standards.

### 5.2.2 Making the standards easy to apply

The current enterprise accounting standards only cover the general enterprise accounting standards and, in the chapter 31, have exemption articles for the SMEs. Therefore, if someone wants to use the exemption articles, he/she has to know all the general articles. Moreover, Hwang et al.(2009) pointed out the SMEs are not using the exemption articles well. This shows that there are difficulties for the SMEs to use the exemption articles. The report on the accounting standards for the SMEs by KBIZ(2011) also pointed out the problems of the standards for the SMEs because it only prescribes exemptions for the SMEs from the general articles. This way requires the person in charge to know all the general articles in the accounting standards so that the accounting personnels in the SMEs are having serious difficulties applying the accounting standards.

Therefore, the SMEs should have its own accounting standards which have enhanced simplicity.

### 5.2.3 Consistent with the tax law

Kim et al.(2009) stated that if the tax law is consistent with the enterprise accounting, the accounting work will be a lot alleviated. Kim et al.(2006) also pointed out the needs for introducing the accounting standards for the SMEs which are consistent with the tax law. Kim(2004) stated that differences between the enterprise accounting and tax accounting make the accounting work difficult. The purposes of both accounting are clearly different but for the accounting transparency improved, there are a lot of parts to accept. Especially, the simplicity of the enterprise accounting should be emphasized by accepting the articles used in the tax law in the accounting standards for the SMEs.

The data from KBIZ(2011) suggests application of the cost basis for asset evaluation, covering securities, inventories, intangible assets and tangible

assets. The method to evaluate the securities in the enterprise accounting standards has two parts; held to maturity and held for trading. When evaluating the held to maturity by acquisition cost after refunding, the difference between the maturity value and acquisition cost should be adjusted by effective interest method during the period of refund. The held for trading and the available for trading are evaluated by the official price. However, if the available for trading doesn't have market value so that the official price can not be fairly evaluated, the acquisition cost is evaluated. In the corporate tax law, the evaluation of the securities is not counted. The enterprise accounting standards use the cost of market method as its principle in evaluating the inventories. The corporate tax law only uses the cost basis but only with previous permission the cost of market method can be used. In reality, there are a few cases the cost of market method is asked. If the accounting standards for the SMEs are applied to evaluate the securities and inventories, the process will be a lot simplified. When evaluating intangible/tangible assets, the impairment losses should be obliged to apply. According to the tax law, the fixed asset shouldn't accept appraisal losses except for the natural disaster but is only evaluated by the cost basis. This can be used in the accounting standards for the SMEs.

Capitalization of interest cost is also important. According to the enterprise accounting standards, the loan cost of inventories is optional to capitalize. The corporate tax law limits the financial cost capitalization to only for the fixed asset for business. So the loan interest of inventories is excluded from the subjects to capitalize and so is for the accounting standards for the SMEs.

The corporate tax law doesn't apply the discounted calculation of purchasing trade of the long term installment but can apply nominal acquisition price to its asset acquisition price. The Chinese accounting standards for the small companies also allow omission of the complicated discounted price calculation since the difference of acquisition price is adjusted during the depreciation. Thus, the cost basis can be applied for the purchased asset of long-term installment. Especially, the acquisition price of the financial lease can be calculated as nominal price.

### 5.3 Strengthening aspect

#### 5.3.1 Reflecting the current state of the SMEs.

The current state of the SMEs should be applied to the accounting standards for the SMEs. Especially, the accurate state of the accounts for the profits and losses should be reflected. To well reflect the state, the frequently used accounts should be defined, The accounts of Deozon Accounting Program, which is widely used among the SMEs, includes payroll, deprivation, rent, repairmen, car maintenance, ordinary R&D, logistics, education&training, printing, meeting, packaging, office supplies, other supplies, commission, inventory, advertising, promotion, bad debt expense, secret, building maintenance, expense for exporting, sales commission, intangible fixed asset expense, exchange commission, sample, order, association fee and others as accounts for profits and losses. There are no detailed descriptions and definitions for the accounts for profits and losses in the current accounting standard. So the accounting standards for the SMEs should give more detailed descriptions of the accounts and definitions of them. The accounting standards for the SMEs should well define employee welfare expense, entertainment expense, benefits, transportation expense, meeting expense since those accounts have grey area in their definitions. In the tax law, entertainment expense includes social expense, commission, meeting and other accounts relevant to these and means the expense corporate spends on the non-work related to operation. The employee welfare expense means the means corporate spends on the welfare of its employees and executives. By well defining these accounts, the current state of the SMEs will be well reflected.

#### 5.3.2 Stipulating the standards about accounting transparency

The standards about accounting transparency should be stipulated for the SMEs in order to secure accounting transparency. The accounting transparency should be secured by introducing necessary process. As Kim et al.(2006) and Kim(2004) showed in their studies, the accounting transparency of the SMEs may decrease the accounting fraud in the society as a whole.

Accounting guide of KBIZ(2011) also puts importance on the accounting transparency of the SMEs. There are contents that have to be stipulated below.

The prohibition of omitting cash-based trade and the prohibition of manipulating fictional cost and suspense account must be stipulated in the accounting standards of the SMEs. The SMEs have more cash-based sales than those of big enterprises. There are few reports about cash-based trade except the credit card reports, debit card reports, tax invoices and cash receipts reported in NTS. For now, the National Tax Service calculated the proportion of cash-based trade of the whole business in the country. If the cash-based sales are relatively lower than those from the credit card, they send modifying recommendations. As use of the credit card increases, the tax revenue and accounting transparency of the SMEs has been a lot increased. Still, there are a lot of omissions of cash-based sales so the standards have to stipulate prohibition of omitting the cash-based sales. In the SMEs, the provisional payment is widely used because the funds of a company is regarded as private funds(a lot of the SMEs are owned by individuals or the major shareholder owns majority of the stocks of a company). However, this exclusive ownership of a company makes the accounting transparency of the SMEs less competitive in the highly competitive market. The level of the employees of the SMEs is getting higher, so they are well aware of the operational state of the SMEs. In the SMEs where the managerial transparency is low, the employees have relative lower loyalty. The fund should be properly traded even though the majority of them is from the major shareholder him/herself alone. By defining the provisional accounts well, the funds of the corporate and the individual are clearly divided. Moreover, the management of the SMEs should have clear responsibility in such areas. Like in the sales in cash, the purchase price in cash should be properly calculated in accounting process. The omission of the purchase price in cash has a lot of side effects. Moreover, the accounts payable cannot be applied so the accounting transparency decreases. The omission of such accounts distorts the profits and losses in the current term which makes the financial sheet and

information of the cash flow useless. The SMEs are always having problems with the cash flow so such financial frauds may put them in a serious danger so the stipulation of processing purchase price in cash should be included in the standards.

On the other hands KBIZ(2011) pointed out the special personnel who don't actually work full time shouldn't be include in the accounts for the benefits or payroll. If such personnel is listed on the payroll but actually don't work in the company, the calculation of payment, social expense and other benefits is prohibited and it should be stipulated as well.

### 5.3.3 Strengthening the managerial accounting report aspect

In the financial sheet of the SMEs, the profitability, the stability, the activeness and the growth of that company should be indicated. In the financial sheet, by indicating the rate of the financial state in the previous and current term, the management can see the actual performance of the company and the direction. For the profitability account, profit rate by sales figure, profit rate by sales, net profit in the current term should be indicated. For the stability account, flexibility rate should be indicated. For the activeness account, turnover rate of the inventories and credit should be indicated. For the provisional growth account, the growth in the sales figure should be indicated. However, the SMEs should learn how to use the financial sheet in management not only for tax report since the environment around them gets worse gradually. Therefore, the key performance index should be managed so that the management can use the financial sheet more effectively. In the study of Kwon and Lee(2010), the rate of use of strategic cost management affects production properties and they affect the performance so that the rate of use of strategic cost management has meaningful relationship with the performance by enhancing the production speed.

## 6. Problems of method to introduce the standards and its counter-measurements

### 6.1 Problem of reflection of the evaluated value and its counter-measurements

Even though the evaluation of the asset on the cost method may distort the value of the asset, the simplicity should be emphasized. If the inventories are evaluated on the cost basis method, the financial sheet may be distorted. However, the general use of the evaluation on the cash basis doesn't have many problems if the exceptional cases are well adjusted in advance. In reality, the SMEs usually don't use the cost of market basis method which may decrease the net profit in the current term so that the cash basis is desirable to use for the SMEs. The normal SMEs don't have a lot of securities and have relatively lower relationship with its work. Therefore, the cost basis method may not distort the actual value in the accounting standards for the SMEs. The cost basis of the intangible/tangible assets is also the problem of the period so it has lower importance.

### 6.2 Problem of distribution and counter-measurements(Establishment of the SME accounting support center)

Once the accounting standards for the SMEs are introduced, it may be hard to distribute the standards and train the professionals. Kim(2004) stated that KACPTA, KICPA, SMBA and universities should give regular training for the SMEs. Kim et al.(2006) stated that SMBC and KCCI should have regular education or training of accounting for the employees in the SMEs so the standards have more effectiveness. Hwang et al.(2008) stated that, in the school education, the subjects regarding the financial fraud should be included so that the financial fraud should be managed systemically.

However, these measurements may vary by the organizations. Therefore, given the importance of the SMEs in the national economy, the SME accounting support center should be established and education and training should be under its control.

## **7. Benefits of introducing the accounting standards for the SMEs.**

The introduction of the accounting standards for the SMEs will have effects below.

First, the simplicity of accounting is increased and it becomes easy to understand so that it becomes easy to train the professionals. Minimizing the standards about evaluation and wide use of the cost basis method will make the standards easy to understand. So far, the SMEs have had trouble understanding and using the enterprise accounting standards because they are too complicated. So it was hard to train the accounting professionals.

Second, it may lead the SMEs make their own financial sheets by themselves. They can make their own financial sheets which they can easily understand. So far, the financial sheets of the SMEs were mainly outsourced so it didn't have enough reliability. So Naturally, the financial agencies had problem trusting the financial sheets of the SMEs. Therefore, it is necessary to enhance capability to settle their finance by themselves

Third, the information provided by the accounting standards for the SMEs will make the management be aware of an accurate state of the company, which will benefit a lot making plans for the future.

Fourth, the investment will increase and resource distribution will be done efficiently due to better reliability of the SMEs' accounting. After the Financial crisis, the stability of the national funds and the needs to distribute the given resource become more important than before. Especially, it is hard to pick which SMEs to support. The accurate financial information generated by the accounting standards for the SMEs will help the companies use the resource more efficiently

## **IV. Conclusion and Acknowledgements**

This study is a research about introducing the independent accounting standards for the SMEs. In the study, the recently introduced institutions

regarding accounting transparency are reviewed and the needs of introducing the institutions are suggested. There are many institutions for the listed companies while the institutions for the un-listed companies are very insufficient. The fact that the SMEs don't have much money to make financial information of them and over-protection of the SMEs decreased the accounting transparency.

The reasons why the study was done are below.

First, the range of the external audit subjects has been decreased; given the situation K-IFRS is shown as difficult to follow. The range of the external audit subjects changed from the whole asset size 7bil won to 10bil won, the number of the subjects dramatically decreased. So the needs to introduce institutions to enhance accounting transparency increased.

Second, the accounting transparency of the SMEs affects that of the large companies. A financial fraud(trade off the sheet) of a company may affect a lot of related contractors.

Third, the demand of the social responsibility of the companies increased a lot. If the accounting transparency of the SMEs is not enhanced, the reliability of a company decreases and the lowered reliability will worsen the image of the Korean companies. The accounting transparency is the first step of a social responsibility of a company.

The institutions taken so far are establishment of KAI, reinforcement of management and supervision of the accounting authorities, institutions to improve the management, obligation of internal control structure, introduction of IFRS, and introduction of inspectors. However those institutions are focused on the listed companies.

Recently, the accounting transparency of the SMEs becomes more and more important. Therefore, this study reviewed the pre-study of the method of securing the accounting transparency and the ways of introducing the accounting standards for the SMEs.

The contributions of this study are like below.

First, the institutions taken to secure accounting transparency were reviewed. The institutions are establishment of KAI, reinforcement of management and supervision of the accounting authorities, institutions to

improve the management, obligation of internal control structure, introduction of IFRS, and introduction of inspectors. The study showed the current institutions are focused on the large companies so the institutions for the SMEs are needed.

Secondly, the foreign cases are reviewed. For now, the accounting system for the small companies is used in China and the accounting for the SMEs is permitted to a certain level in America. Here, the study also showed the needs for introduction the accounting standards for the SMEs.

Third, the concrete methods for the accounting standards for the SMEs are suggested. Even though, there have been studies regarding the accounting standards for the SMEs, there were no concrete methods for them. The study covered two parts; one is to be alleviated and the other is to be strengthened.

The acknowledgements of the study are like below.

First, the study doesn't cover the individual acts of the standard but just suggest the contents that should be included and the method to introduce it, based on the foreign cases and the pre-studies. The independent accounting standards may need more detailed guides. Later, it is needed to study more detailed articles.

Second, the study by quantitative research method on the accounting standards for the SMEs should be added. Based on the introductory methods for the accounting standards for the SMEs, the reliability of the financial sheets and the levels of hindrance of evaluation of a companies should be studied more in detail.

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## Abstract

### 회계투명성관련 제도와 중소기업회계기준의 도입

박상섭\*

본 연구는 중소기업에 대한 회계투명성 제고를 위하여 독립된 중소기업회계기준의 도입의 필요성을 제기하고, 독립된 중소기업회계기준의 도입에 대한 방향을 제시한다. 정부는 상장기업을 중심으로 회계투명성 관련 제도를 지속적으로 도입하였다. 그러나 상대적으로 비상장 중소기업의 회계투명성의 제고를 위한 제도의 도입은 매우 적다. 중소기업의 회계투명성제고를 위하여 중소기업이 이해하고 활용할 수 있는 중소기업회계기준의 도입이 반드시 필요하다

따라서 본 연구에서는 최근 도입된 회계투명성 관련 제도를 살펴보고, 중소기업의 투명성제고 방안과 관련된 선행연구를 살펴보았으며, 독립된 중소기업회계제도의 도입 방안을 살펴보았다.

독립된 중소기업회계기준의 도입을 위하여 현행회계기준의 문제점 및 중소기업회계기준의 필요성을 설명하고, 외국의 중소기업회계제도에 대하여 살펴보았다. 중소기업회계기준의 도입방안으로 완화방안과 강화방안을 제시한다. 완화방안으로는 이해용이성의 향상, 적용간편성의 증대, 세법과의 일관성 확보의 방안을 제시하였다. 강화방안으로 중소기업의 실상반영, 회계투명성관련 기준의 명문화와 관리적 회계보고측면의 강화의 방안을 제시하였다.

추가적으로 독립된 중소기업회계기준의 도입방향의 문제점과 대책을 기술하고, 보급방안을 제시한다.

핵심주제어 : 회계투명성, 중소기업회계기준, 소기업회계제도, 중소기업 회계처리특례

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