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LAW ON ACCOUNTING IN THE REPUBLIC OF SERBIA AND APPLICATION OF IAS/IFRS

ABSTRACT: In accordance with its legal accounting framework, the Republic of Serbia has adopted IAS/IFRS as the sole financial reporting framework for all entities, while taking into account certain formal specificities of medium-sized and small enterprises. The International Accounting Standards Board (IASB) played a key role in this approach. These initial observations aim to highlight the quality of financial statements as a result of the application of the current accounting legislation in the Republic of Serbia.

The issue of comparability and harmonization of financial statements is particularly relevant to medium-sized and small enterprises, as well as to companies whose securities are listed on the stock exchange. Research findings suggest that the application of the existing legal framework—specifically the mandatory and exclusive use of IFRS—has become a limiting factor in the quality of financial statements and, consequently, their representational value.

The thematic scope of this paper involves the application of a methodology based on the collection of secondary data from relevant domestic and international sources. Through processing and analysis, this information enables an assessment of the current state of financial reporting quality.

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From the perspective of financial information users—primarily investors and creditors—the second part of the paper presents research findings and proposes measures to improve accounting regulations with the aim of enhancing the quality of financial statements.

Keywords: *law on accounting, accounting regulations, financial statements, EU Directive 34.*

1. Introduction

The organization of a company's accounting function is conditioned by the applicable normative accounting regulations. Depending on who regulates and prescribes the accounting framework, it can be classified as: statutory regulations prescribed by the state or authorized state institutions; professional regulations developed and promoted by professional organizations; and internal accounting regulations created by companies (internal acts) in compliance with statutory and professional regulations. The scope of statutory accounting regulations fundamentally covers all segments of corporate accounting, with particular attention to accounting procedures and financial reporting. Statutory regulation of accounting serves as a fundamental assumption for ensuring the quality of financial statements and enhancing their informational power in line with the needs of financial information users. This highlights the importance of normative regulation in accounting. Modern statutory accounting regulations enable the accounting system to achieve a high degree of standardization, ensure the quality of financial information, and fully disclose transactions for the needs of strategic management. In other words, the accounting system, or the financial reporting system, is directly influenced by statutory accounting regulations.

The primary objective of this paper is to highlight the current level of harmonization in accounting practices and explore new trends in statutory accounting regulations that explicitly impact the quality of financial statements. Specifically, it focuses on creating financial statements that encompass both financial and key non-financial information, which define a company's growth and development. This involves formulating a new financial reporting system that complements traditional financial reporting with metrics driven by the enablers of future performance in value creation for the company. As noted by Anđelković (2020) "Information of a non-material nature from financial statements is of great importance for establishing a relationship of dependence between customers and companies in order to create and increase the value of the firm"(pp. 43–58).

In line with the stated research objective, the hypothesis is set that there is a real need for users of information to innovate the structure of financial statements, which will comprehensively cover both the financial and non-financial perspectives of an entity's operations. This structure should be based on key success factors that include both financial information and information related to technology and innovation, customer satisfaction, and other non-financial information. The focus of the research is directed toward new, modern regulations, which result in more comprehensive financial statements aimed at increasing their quality and informative value for strategic decision-making. According to Palea (2018), a group of high-ranking experts on sustainable finance (HLEG, 2018) pointed to the need for better consideration of sustainability issues in accounting standards. All of this leads to the formulation of a financial reporting model that emphasizes the necessity of revising statutory and, consequently, professional accounting regulations.

2. The Quality Status of Financial Statements as a Result of the Application of Statutory Accounting Regulations

The organization of a company's accounting function is significantly influenced by the applicable normative framework, with the legal accounting regulations being the fundamental factor. Legal regulations essentially cover all segments of corporate accounting, with special attention focused on accounting procedures and financial reporting. In preparing financial statements, the importance of normative regulation is emphasized to ensure complete and reliable information about the economic and financial position, as well as the performance of a company, for both external and internal reporting purposes. According to the Accounting Standards Board (ASB) headquartered in the United Kingdom, as well as other regulatory accounting standards bodies, the objective of financial reporting has essentially remained unchanged. When preparing financial statements, the importance of normative regulation is emphasized to ensure complete and truthful information about the economic and financial position and the business success of enterprises for the needs of external and internal reporting. The financial statements should provide such information that offers a framework through which significant information obtained from specific sources is illustrated (Bromowich, 2001, pp. 47–72).

Financial reporting can be normatively regulated in several ways, including:

- Statutory regulations, such as the law on entities and accounting principles;
- Supplementary regulations of competent state financial institutions;
- Stock exchange rules and normative regulations concerning the exchanges issued by the government;
- Accounting guidelines and standards issued by accounting professional bodies (Alexander & Nobes, 2010, p. 48).

The international variation in the nature of legal systems often affects how accounting regulations are interpreted in different countries. National economies are characterized by basic systems related to the "Roman law codified system" and "common law" (general legal approach). In many countries, especially in Western Europe, the legal system is based on Roman law. The term "codified" is associated with this observation. Principles or postulates directly influence the definition of rules related to accounting and finance and impact the nature of regulations in a given country.

Research results indicate that the most common differences in financial reporting in a given country result from differing approaches to normative regulation in other countries regarding the law on accounting and the definition of professional accounting regulations. Similarly, different countries have varying approaches to sources of financing, tax systems, macroeconomic analyses of economic trends, and microeconomic analyses. Differences in the development of accounting practices are also evident. When it comes to the Republic of Serbia and its Accounting Laws (2013), accounting regulation is partly the result of the international environment and its regulatory body that has defined IAS/IFRS. Financial statements that are comparable with those of other enterprises are considered important instruments for protecting the interests of investors and creditors. However, it should be noted that the statutory accounting regulations in the Republic of Serbia must also reflect other environments, particularly in relation to continental European countries. Additionally, accounting regulations should take into account the specificities of the Republic of Serbia, which are reflected in its customary accounting practices. This is supported by numerous facts. One such fact relates to the country's legal and tax system. Similarly, different countries have different financial institution structures and sources of financing. Therefore, each country is inevitably faced with the fundamental question of shaping financial statements to ensure their quality and alignment with the needs and interests of financial information users. According to the aforementioned Accounting Law (2013), information for strategic management purposes is derived from the following set of financial statements: the Balance Sheet and the Income Statement as the fundamental financial statements regarding the profitability and financial performance of enterprises; the Statement of Other Comprehensive Income; the Statement of Changes in Equity; the Cash Flow Statement; and the Notes to the Financial Statements, which are crucial for assessing the financial position and performance of enterprises. With the adoption of the Law on Accounting (2021), efforts to achieve complete harmonization of financial reporting have continued.

In the Republic of Serbia, with the adoption of the Accounting and Auditing Law (2006), further efforts were made to organize the accounting profession and achieve complete harmonization with international accounting regulations. International Accounting Standards and International Financial Reporting Standards (IAS/IFRS) represent the primary basis for the highly significant global process of harmonizing financial reporting. As noted by Dmitrović, Petković & Jakšić (2012) "The harmonization of financial reporting requires accounting to provide a more efficient understanding of the financial position of large companies (and other business entities) to ensure greater capital protection and reduce investment risk. At the global level, certain accounting rules have been established to achieve comparable financial statements" (p. 23).

When it comes to activities defining professional regulations, Barth, Landsman, Lang and Williams (2012) emphasize the influence of prominent accounting institutions worldwide, which have contributed to the global application of unified accounting rules contained in professional regulations. Based on legal provisions, our country has adopted an accounting framework that applies entirely to economic entities. The exception applies to small legal entities, which may choose not to apply IFRS if their securities are not traded on an organized securities market (Accounting and Auditing Law, 2006, Article 25). Micro-entities and entrepreneurs apply a bylaw issued by the minister responsible for financial affairs, which is based on general accounting principles. Medium-sized companies may apply IFRS that are valid for large legal entities. The aforementioned facts regarding statutory accounting regulations indicate that, in addition to the state, another highly significant guiding force in statutory regulation pertains to the accounting profession. Confirmation of this position can also be found in the new Accounting Law, more precisely in the part that regulates the issue of professional regulation (Accounting and Auditing Law, 20006, Article 2, Paragraph 4).

3. Improvement of Legal Accounting Regulations for the Purpose of Financial Report Quality

In previous discussions related to legal accounting regulations as determinants of professional regulation, the focus of the research was on traditional, classical financial statements. However, in a modern business environment, strategic management primarily focuses on strategic success measures, many of which are non-financial performance measures, such as research and development of new products, innovations, knowledge, customer satisfaction, etc. As Vunjak and Ostojić (2014) note, what is crucial from the perspective of strategic management is that "Financial reporting and operations must consider not only financial indicators but also other indicators unrelated to financial performance." Managers increasingly recognize the limited usefulness of information derived from financial statements for strategic management purposes, proposing a revision of legal accounting regulations. Palea (2018) cites Gauzès (2017), where it is stated that the "chairman of the board of the European Financial Reporting Advisory Group highlighted the need to overcome the traditional, classical approach focused on 'technical accounting.'" According to Dečman (2013) "it can be concluded that accountants are more devoted to performing traditional tasks (preparing financial statements, cost-financial control) while their involvement in planning, and especially decision-making, is less prominent" (p. 533).

A new financial reporting system for strategic management should include both financial and non-financial parameters (Škrinjar, Bosilj-Vukšić & Indihar-Štemberger, 2008, pp. 738–754). It is well known that information obtained from accounting information systems is often the basis for making business decisions. In addition to these, non-accounting information plays a particularly significant role in strategic management, as emphasized in recent years. In this context, it is necessary to explore a new approach to financial reporting for strategic management purposes. A revision of legal regulations, existing IFRS, and the broader impact of IFRS on the economy should be considered.

The revision of accounting regulations requires a preliminary approach to assessing the current state of accounting practices and previously established regulations in the field of accounting. This would contribute to defining new legal regulations that would enable the creation of comparable financial statements as a means of communication between enterprises in EU member states. Even if financial statements do not contain all the necessary information, they still provide users with a framework to compare certain data with other sources (Kothari & Barone, 2012, p. 1). The International Federation of Accountants (IFAC) plays a key role in defining standards and postulates, which is particularly important for harmonizing accounting and financial reporting practices. If financial statements lack the necessary information, they still provide a framework for users to compare (Barone & Kothari, 2012, p. 1). The International Federation of Accountants (IFAC) plays a key role in this process by setting accounting principles and standards, thereby significantly harmonizing accounting systems and financial reporting practices. According to legal provisions in our country, the application of professional IAS/IFRS regulations does not consistently address the issue of company size or whether a company is listed on the stock exchange, particularly when it comes to the interests of small and micro-entrepreneurs regarding regulatory burdens. According to Mamić, Dečman and Sever (2015) "empirical research has confirmed that simplifying accounting regulations is justified, especially for small businesses, as it would reduce costs. At the same time, the quality of information will not be diminished due to the simplification of accounting regulations" (pp. 593–607).

Furthermore, the accounting regulatory standards in the Republic of Serbia are not harmonized with key aspects of the European Union's Directive 34. This significantly affects the quality of financial statement information in terms of comparability with the financial statements of other participants in the international market, particularly those listed on the stock exchange. According to Dragojevic, Miljevic & Milojevic, (2012) IFRS was supposed to provide a precondition for applying an explicit approach to positions from financial statements that would contribute to higher quality from the perspective of information users (p. 203).

Moreover, accounting regulations in our country have not taken into account the country's rich accounting history and, therefore, the existence of its own national accounting system. Another fundamental aspect of improving statutory and professional accounting regulations to enhance the quality of financial statements stems from modern empirical research on accounting practices. The research results indicate the need to revise the existing statutory and professional accounting regulations, to create more comprehensive financial statements that would meet the increasingly complex needs of information users for strategic management. Financial and non-financial information for strategic management purposes holds different significance depending on whether the focus is on large and medium-sized enterprises or small entrepreneurs. Statutory accounting regulations, as a prerequisite for the quality of financial statements for strategic management purposes, must take this into account. Large, medium-sized, and small enterprises are distinct entities in terms of the organization and regulation of financial reporting. This primarily applies to external users (mainly investors and creditors). Therefore, the question arises of the extent to which small and medium-sized enterprises use such information for strategic management purposes in the context of improving their business quality. It is necessary to explore alternative performance measurement systems that would complement financial statements. To emphasize the importance of using strategic information, both financial and non-financial, accounting reports on enterprise performance should now be based on critical success factors of the enterprise. These factors should encompass not only the financial perspective but also customer satisfaction, new technologies, internal processes, and development.

The business decision-making level requires setting objectives aimed at increasing revenue sources by expanding the product range with new products and services. From the perspective of customer satisfaction, creating elements that increase their value is of primary importance. As noted by Anđelković and Vujić (2019) "Measuring customer profitability introduces another key determinant in a company's operations. This establishes a dependency and connection between factors that determine the company's operations as a result of financial performance and other factors, such as customer satisfaction, which are not financial in nature. All this contributes to increasing the company's value" (pp. 414–431).

Since customers are directly or indirectly linked to every activity that creates value for the company, the value of customer relationships should be analyzed in the same way as business operations. According to Barone & Kothari (2012) David Packard, co-founder of Hewlett-Packard, stated: "Profit is not the proper goal or purpose of management, it simply makes all other goals and purposes achievable"(p. 11). His vision emphasized that the true purpose of a business is to create value for its customers, with profit being a result of achieving that goal (Magretta, 2002, pp. 86–92). Vuković, Vukić and Sesar, (2020) further assert that "Non-financial reporting includes information on relevant measures affecting business development and results, as well as the social and environmental impact of operations. It provides essential tools for understanding development, business results, and the enterprise's position (pp. 41–58). Market and regulatory frameworks significantly influence the revision of legal regulations in modern business practices. This has led to the need for an integrated approach in creating enterprise value. The new influence on performance analysis and strategic management systems includes financial calculations alongside non-financial perspectives of the company, bringing them into direct interdependence with finance. Cvitanović (2018) in the context of non-financial determinants that influence a company's business results, particularly emphasizes the "role of marketing and its interaction with other functions within the enterprise. The integrated approach to financial reporting also includes elements related to the intersubjective construction of value (pp. 83–94). Various strategic variables influence the measured values of financial statement information. Among the analyzed strategic variables that enhance financial indicators are research and development, innovation, knowledge, and customer satisfaction. Modern accounting regulation research demonstrates the necessity of including non-financial performance measures in financial reports. In this context, Bernard and Roland (2016) emphasize the need to reassess the current domain of finance in light of the importance of financial report information within the "new perspective of sustainable finance" (p. 441). This approach would provide a more accurate informational basis for strategic management needs. Consequently, the new approach introduces financial calculations into other dimensions of the enterprise, fostering a dialogue between these dimensions and finance. Based on the above, it can be concluded that, alongside the conventional or classical financial reporting approach supported by AISB's IAS/IFRS project. Research in this paper also highlights another system of interdependent performance measures, which stress the need for a revision of financial statement quality.

Progress linked to the aforementioned conventional financial reporting approach can be observed in one of the sets of financial statements prescribed by IAS/IFRS, which relates to "Notes to the Financial Statements" (Accounting Law, 2019). The impact of the notes is significant, as they increase the informational power of the data contained in the financial statements related to "Disclosures." In this way, users of financial statements gain a clearer picture of the financial, asset, and income position of each company. Regarding this observation, Anđelković (2020) states "The information disclosed in notes as part of financial statements, which results from the financial and non-financial performance of an enterprise, is of particular importance for objectively determining current business results, especially for making strategic decisions in the future" (pp. 46–47).

4. Conclusion

Legal accounting regulations represent a prerequisite for defining professional accounting directives and, thus, a fundamental determinant of the quality of financial reporting. The research results point to certain issues in the application of existing legal provisions in our country. On the one hand, their application, which forms the basis of professional regulation, represents a significant regulatory burden for some enterprises in terms of their size. On the other hand, the creation of financial statements as a result of legal regulations does not account for a complex, integrated approach to information that shapes a company's financial results. This conclusion arises from the fact that our country, based on legal provisions, implemented only one area of international standards in the creation of financial statements without considering key accounting standards from other international sources. This particularly applies to Directive 34 and generally accepted accounting principles (US GAAP). Additionally, Serbia's accounting regulation did not take into account its rich accounting practice.

We believe that for the purposes of strategic management, it is necessary to supplement financial statements with alternative and mutually conditioned business performance indicators in accordance with generally accepted accounting principles (US GAAP) and the International Federation of Accountants (IFAC), which has established accounting postulates through its standards, thereby harmonizing the system for preparing and presenting financial statements. Contemporary trends indicate that International Financial Reporting Standards (IFRS) and EU directives are undoubtedly the most significant acts. This stems from the fact that most countries with professional regulations defined by the Accounting Law align their accounting rules in significant matters with these standards. In the context of financial reporting quality, it is viewed from the perspective of international accounting harmonization and, consequently, national alignment of the financial reporting system. The balanced scorecard model is a good example of an integrated performance measurement system that, among other things, serves to implement strategic intentions and predict the future. Business uncertainty and the turbulent environment in which companies operate have imposed a complex model of interrelated components in the creation of accounting reports for the needs of strategic management. Research results verify the hypothesis that strategic management will rely on financial reports which, on one hand, will encompass the financial dimension of the company's operations, and on the other hand, factors that are non-financial in nature. In this context, the concept of sustainable finance is understood as an informational support for strategic management.

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ZAKON O RAČUNOVODSTVU REPUBLIKE SRBIJE I PRIMENA MRS/MSFI

APSTRAKT: Republika Srbija je u skladu sa svojom zakonskom računovodstvenom regulativom usvojila MRS/MSFI, kao jedini okvir finansijskog izveštavanja za sve subjekte, uzimajući u obzir formalne specifičnosti srednjih i malih preduzeća. Ključnu ulogu u ovakvom pristupu imao je Međunarodni odbor za računovodstvene standarde (IASB). Prethodne konstatacije imaju za cilj da ukažu na kvalitet finansijskih izveštaja kao rezultat primene postojećih zakona o računovodstvu Republike Srbije. Problem uporedivosti i harmonizacije finansijskih izveštaja naročito se odnosi na srednja i mala preduzeća, kao i na kompanije čije se hartije od vrednosti nalaze na berzi. Rezultati istraživanja ukazuju da je primena postojećih zakonskih propisa, odnosno zakonske računovodstvene regulative koja reguliše direktnu i isključivu primenu MSFI, postala ograničavajući faktor kvaliteta finansijskih izveštaja, a samim tim i njihove reprezentativne vrednostii. Tematska oblast rada definiše primenu metodologije koja se zasniva na prikupljanju sekundarnih informacija iz domaćih i međunarodnih relevantnih izvora. Kao rezultat njiihove obrade i analize dobijaju se informacije koje nam omogućavaju sagledavanje postojećeg stanja kvaliteta finansijskih izveštaja. Sa aspekta korisnika finansijskih informacija (pre svega investitora i poverilaca), u drugom delu ilustracije rada ukazuje se na rezultate istraživanja i predlog mera za unapređenje računovodstvenih propisa kako bi se poboljšao kvalitet finansijskih izveštaja.

Ključne reči: *Zakon o računovodstvu, računovodstveni propisi, finansijski izveštaji, Direktiva 34 EU.*

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