Winter 2017

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Recommended Citation

Ward, C.L. & Lowe, S.K. (2017) Cultural impact of international financial reporting standards on the comparability of financial statements. International Journal of Business, Accounting, and Finance, Vol. 11 (1), 46-56.

CULTURAL IMPACT OF INTERNATIONAL FINANCIAL REPORTING STANDARDS ON THE COMPARABILITY OF FINANCIAL STATEMENTS

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ABSTRACT

Due to globalization and expanding international business, it has become necessary for companies in various countries to communicate through a universal language of accounting. International Financial Reporting Standards (IFRS) were developed and issued to serve as a uniform set of accounting standards. A proposed advantage of global implementation is the improved comparability of financial statements. However, due to variations among cultures, it is unrealistic for a single set of standards to be accepted and implemented in a wholly uniform manner to produce innately comparable financial statements. Because of cultural differences, there are varying degrees of IFRS acceptance: some countries adopt the full set of IFRS, while others only accept certain standards. The application of the standards in various countries could adversely impact the comparability of financial statements. Hofstede's cultural dimensions aid in understanding the differences among cultures, the impact this can have on financial reporting, and therefore the comparability of financial statements prepared using IFRS. Through a series of independent t-test analyses, this study finds that two of Hofstede's cultural dimensions—power distance and individualism—are found to be significant, suggesting that these values influence a country's acceptance of IFRS as issued by the International Accounting Standards Board (IASB).

Keywords: *Culture, international financial reporting, comparability, financial statements*

INTRODUCTION

International business is growing and expanding rapidly due to globalization. With increasing global business interaction, it is necessary for companies in various nations to communicate through a universal language of accounting. In response to this need, the International Accounting Standards Board (IASB) developed International Financial Reporting Standards (IFRS). It is expected that IFRS will become the uniform set of global accounting standards. Universal implementation of IFRS would be advantageous in areas such as financial statement comparability, raising capital abroad, and reporting within multinational corporations (Elena et. al., 2009). Currently, over 140 nations and jurisdictions require or permit IFRS (IFRS Foundation, 2015).

The European Union adopted IFRS in 2005, which was a milestone for both the IASB and IFRS. This required nearly 7,000 companies in the 25 countries of the European Union to simultaneously shift from national Generally Accepted Accounting Principles (GAAP) to IFRS (Pacter, 2015). Since that time, many other nations have adopted IFRS or begun to converge their existing accounting standards with the global standards. Such countries include Canada, Mexico, and Russia. The United States still predominantly uses United States GAAP, but the Securities and Exchange Commission (SEC) has implemented a work plan for the consideration of incorporating IFRS into the US financial reporting system (Securities and Exchange Commission, 2012).

Opponents of IFRS purport that the standards represent an Anglo-American tradition that may be perceived as irrelevant in nations with substantially different cultures (Borker, 2013). Due to variations among cultures, it is unrealistic for a single set of standards to be accepted and implemented in a wholly uniform manner to produce innately comparable financial statements.

The purpose of this study is to determine the possibility of whether or not a country's cultural profile influences its acceptance of IFRS as issued by the IASB. This research contributes to the literature by expanding prior research and analyzing the cultural indices of three groups of countries.

LITERATURE REVIEW

Since the implementation of IFRS, many studies have focused on the cultural acceptance of the new standards. Cultures differ among nations, and accounting principles are affected by the culture of the people implementing them. Simply changing accounting standards does not change the thought patterns and underlying decision making processes of the respective accountants (Cieslwewicz, 2014).

Based on the study by Nobes (2011) "accounting practices flow from deep-seated and long-lasting national influences" (p. 15). Therefore, these practices are resistant to change, even if it is considered to be harmonization (Nobes, 2011). Similarly, due to this deep-seated cultural impact, many firms continue to use accounting practices required by former national rules, even after the adoption of IFRS (Haller & Wehfrizt, 2013). This is because culture is interwoven into the accounting business environment, training, and application of standards (Buys, Schutte, & Andrikopoulos, 2012). Even in countries that require IFRS for listed companies, IFRS is often prohibited for private companies. This shows that IFRS does not permeate the culturally accepted accounting principles that have already been in place.

According to Cieslewicz (2014), relationships exist among culture, institutions, and accounting. National culture impacts the institutions of a nation, which impact the accounting framework of the nation. Therefore, simply adopting IFRS is not likely to permanently improve the financial reporting quality of a nation. This is evidenced by a study of comparability of IFRS in German and French firms in the years immediately after the European Union adopted IFRS. Book values in 2006 were more comparable between firms in the two countries; however, book values in 2007 and 2008 were significantly less comparable (Liao, Sellhor, & Skaife, 2012).

Because IFRS is principles-based (as opposed to rules-based), there is a broad scope for exercising professional judgment (Benston, Bromwich, & Wagenhofer, 2006). The standards rely heavily on a conceptual framework, which is ideally flexible enough to accommodate the evolution of IFRS (Gebhardt, Mora, & Wagenhofer, 2014). As evidenced in the instructional case study by Portz and Strong (2014), financial statement comparability can be impacted by judgements, estimates, and accounting choices—even when using a single set of accounting standards—due to differences in cultural background and the effect this has on the accounting decisions made by management.

Because IFRS allows a degree of reporting discretion, there could be comparability inconsistencies related to estimates such as salvage value, useful life, and bad debt expense. In addition, management's decisions could cause financial statements to be incomparable in instances of recording a lease (operating or financial) or how a potential lawsuit should be disclosed or reported (Portz & Strong, 2014). Similarly, Doupnik (2003) found that interpretation and application of standards are most influenced by culture in scenarios that require judgment.

Determining whether or not to disclose an item is an example of such a scenario. Because the culture of Greece prefers confidentiality, Greek accountants are less likely than American accountants to disclose contingent assets and liabilities (Tsakumis, 2007). Similarly, a study of Chinese and Australian accounting students showed that the Chinese were less likely to fully disclose items in compliance with IFRS (Chand, Cummings, & Patel, 2012).

Because of cultural differences, there are varying degrees of IFRS acceptance: some countries adopt the full set of IFRS, while others only accept partial standards. When adopting International Financial Reporting Standards, individual countries often make modifications. As a result, not each country that claims to utilize IFRS actually uses the international standards issued by the IASB (Obradovic, 2014).

Much of the available literature regarding the cultural implications on IFRS implementation consists of studies using Hofstede's cultural dimensions. Hofstede determined measurable variations that distinguish and differentiate cultures. In 1980, Hofstede proposed four cultural dimensions that have been widely used in a broad range of studies that include cultural factors (Hofstede, 2011). In addition, the cultural dimension model has been used extensively to research and implement practices in business management and organizational culture (Tsakumis, Campbell, & Doupnik, 2009). The original four cultural dimensions are as follows:

1. Power distance: the degree to which less powerful individuals accept the unequal distribution of power;
2. Individualism: the extent to which people are integrated into social groups;
3. Uncertainty avoidance: the degree to which people are comfortable with ambiguity; and
4. Masculinity: the degree to which people are competitive and assertive (Hofstede, 2011).

Based on cultural variances, a country may implement a version of IFRS that does not consist of the same principles issued by the International Accounting Standards Board. This can happen in several different ways: endorsing IFRS, but allowing for some differences; converging standards over a period of time, instead of adopting; or allowing firms to report under either IFRS or national GAAP (Zeff & Nobes, 2010). Table 1 exhibits some of the variations in IFRS among countries that did not adopt IFRS as issued by the IASB.

Table 1
Variations in IFRS as Adopted Locally in Select Countries

Country	Local IFRS Variations
Australia	Did not adopt IAS 26, *Accounting and Reporting by Retirement Benefit Plans*
New Zealand	Some reporting entities ("tier 2 entities") have reduced disclosure requirements
Philippines	Modification of IFRS that impacts the real estate industry; Local IFRS provides guidance for insurance companies, mining companies, and banks
Sri Lanka	Uses a modified standard with respect to some right of use land on lease
Taiwan	Eliminates the option to revalue property, plant, and equipment, intangible assets, and exploration and evaluation assets through other comprehensive income
Venezuela	Requires price-level adjusted financial statements if inflation rate is greater than or equal to 10%, regardless of IAS 29 implications

Source: IFRS Foundation

METHODOLOGY

Sample and Data Collection

For this study, the Hofstede cultural values of 65 countries were analyzed. This data, which is secondary in nature, was collected from Hofstede's collaborative research based on the cultural dimensions he previously developed (Hofstede, Hofstede, & Minkov, 2010). The countries were divided into three categories: countries that do not use IFRS, countries that use IFRS as issued by the IASB, and countries that use IFRS as adopted locally. The following tables display this information.

Table 2
List of Countries that Do Not Use IFRS

Country	Power Distance	Individualism	Uncertainty Avoidance	Masculinity
Bhutan	94	52	32	28
Burkina Faso	70	15	50	55
Cape Verde	75	20	15	40
Egypt	70	25	45	80
Ethiopia	70	20	65	55
Indonesia	78	14	46	48
Iran	58	41	43	59
Senegal	70	25	45	55
South Korea	60	18	39	85
Suriname	85	47	37	92
Vietnam	70	20	40	30

Table 3
List of Countries that Use IFRS as Issued by the IASB

Country	Power Distance	Individualism	Uncertainty Avoidance	Masculinity
Albania	90	20	80	70
Canada	39	80	52	48
Colombia	67	13	64	80
Costa Rica	35	15	21	86
Ecuador	78	8	63	67
El Salvador	66	19	40	94
Jordan	70	30	45	65
Kenya	70	25	60	50
Lebanon	75	40	65	50
Malawi	70	30	40	50
Nigeria	80	30	60	55
South Africa	49	65	63	49
Tanzania	70	25	40	50
Ukraine	92	25	27	95
Zambia	60	35	40	50

Table 4
List of Countries that Use IFRS as Adopted Locally

Country	Power Distance	Individualism	Uncertainty Avoidance	Masculinity
Australia	36	90	61	51
Austria*	11	55	79	70
Belgium*	65	75	54	94
Bulgaria*	70	30	40	85
Croatia*	73	33	40	80
Czech Republic*	57	58	57	74
Denmark*	18	74	16	23
Estonia*	40	60	30	60
Finland*	33	63	26	59
France*	68	71	43	86
Germany*	35	67	66	65
Greece*	60	35	57	100
Hungary*	46	80	88	82
Iceland*	30	60	10	50
Ireland*	28	70	68	35
Italy*	50	76	70	75
Latvia*	44	70	9	63
Lithuania*	42	60	19	65
Luxembourg*	40	60	50	70
Malta*	56	59	47	96
Netherlands*	38	80	14	53
New Zealand	22	79	58	49
Norway*	31	69	8	50
Pakistan	55	14	50	70
Philippines	94	32	64	44
Poland*	68	60	64	93
Portugal*	63	27	31	99
Romania*	90	30	42	90
Slovakia*	100	52	100	51
Slovenia*	71	27	19	88
Spain*	57	51	42	86
Sri Lanka	80	35	10	45
Sweden*	31	71	5	29
Taiwan	58	17	45	69
Thailand	64	20	34	64
Turkey*	66	37	45	85
United Kingdom*	35	89	66	35
Venezuela	81	12	73	76
Vietnam	70	20	40	30

**Denotes countries that, as part of the European Union, adopted IFRS as issued by the EU.*

Data Analysis

The four independent samples *t*-test analyses compare the following cultural values: power distance, individualism, uncertainty avoidance, and masculinity. The *t*-tests were conducted to compare the mean cultural values of two groups: countries who use IFRS as issued by the IASB and countries who adopted IFRS locally. A significant test indicates the possibility that one of the cultural values influences a country's acceptance of IFRS as issued by the IASB.

RESULTS OF THE STUDY

The independent samples *t*-tests were conducted, and the results follow. The first cultural value tested was power distance, and the *t*-test was found to be significant. The results are presented in Table 5.

Table 5
Results of *t*-test Analysis (Power Distance)

Country Group	Mean	Standard Deviation	*t*-statistic	*p*-value
IFRS as Issued by IASB	67.4	16.3	2.61	0.014
IFRS as Adopted Locally	53.2	21.4		

The second cultural value tested was individualism, and the *t*-test was found to be significant. The results of this *t*-test are presented in Table 6.

Table 6
Results of *t*-test Analysis (Individualism)

Country Group	Mean	Standard Deviation	*t*-statistic	*p*-value
IFRS as Issued by IASB	30.7	19.2	-3.66	<.01
IFRS as Adopted Locally	53.0	22.5		

Uncertainty avoidance was then tested, but was found to be insignificant. The results of the *t*-test are presented in Table 7.

Table 7
Results of *t*-test Analysis (Uncertainty Avoidance)

Country Group	Mean	Standard Deviation	*t*-statistic	*p*-value
IFRS as Issued by IASB	50.7	16.1	1.07	0.290
IFRS as Adopted Locally	44.6	23.7		

Finally, masculinity was tested, and it was found to be insignificant. The results of the *t*-test are presented in Table 8.

According to the results of this study, the *t*-test analysis for power distance was significant, indicating that the difference between the means of the two groups of countries was

substantial. As defined by Hofstede, power distance is the extent to which the less powerful members of society accept the unequal distribution of power.

Table 8
(Masculinity)

Country Group	Mean	Standard Deviation	*t*-statistic	*p*-value
IFRS as Issued by IASB	63.9	17.3	-0.44	0.665
IFRS as Adopted Locally	66.4	21.1		

DISCUSSION

A low power distance value indicates that members of society think that power should be used legitimately, and subordinates should be consulted. In such cultures, children are treated as equals to their parents, majority vote changes government aspects, corruption is fairly rare, and income distribution is somewhat even. A high power distance value indicates that members of society think that power should exerted and used for good or evil, whether the power is legitimate or not. In such cultures, children are taught obedience, government aspects are changed by revolution, scandals and corruption are frequent and kept secret, and income distribution is greatly uneven (Hofstede, 2011).

Table 5 shows that countries using IFRS as issued by the IASB have a significantly higher mean value for power distance than do the countries that use IFRS as adopted locally. This indicates that countries using IFRS as issued by the IASB have societies in which there is a greater gap between low power and high power members of society. In such cultures, secrecy is more common, which affects disclosure on financial statements (Dahawy, Merion, & Conover, 2002). Therefore, the same item could be disclosed differently in a country with high power distance and a country with low power distance, affecting the comparability of financial statements.

Individualism (versus collectivism) describes the degree to which members of society are unified in groups. A high individualism value would indicate that members of society value privacy, care mainly for one's self and one's immediate family, and personal opinion is highly important. A low individualism value would be representative of collectivism within a society, indicating that there is a societal stress on feeling as though one belongs, members of society care for extended families, and value is placed on the group as a whole rather than the individual (Hofstede, 2011).

Table 6 shows that countries using IFRS as issued by the IASB have a significantly lower mean value for individualism. This indicates that countries using IFRS as issued by the IASB are more collective. In collective societies, the opinion of the group is more important than the opinion of an individual. This could become troublesome if members of an organization's management attempt to persuade an accountant to report false information. China's collectivist society is greatly influenced by the cultural influence of *guanxi*, which is a Confucian teaching based on the value of relationships. In a society with such importance on collectivism, the principles of objectivity and independence can be more easily compromised (Xu, 2014). Lack of independence and objectivity can affect financial reporting, and thus the comparability of financial statements among countries with varying degrees of individualism.

Uncertainty avoidance describes the degree to which a society is comfortable with ambiguity, or unstructured situations. A low uncertainty avoidance value indicates that members of society accept and welcome the inherent uncertainties of life. People have lower stress, are curious of differences, dislike rules, and are more comfortable which chaos. A high uncertainty avoidance value indicates that members of society feel threatened by life's uncertainties, suffer from stress and anxiety, and need structure and rules (Hofstede, 2011). According to the *t*-test conducted for uncertainty avoidance, there is no significant difference between the means of countries using IFRS as issued by the IASB and countries using IFRS as adopted locally.

Masculinity (versus femininity) describes the degree to which a society is competitive and assertive. A low masculinity value indicates that there is a lower differentiation between emotional and social role in regard to different genders. The following aspects are characteristic of such a society: work-life balance is important, members of society are sympathetic toward the weak, women are involved in politics, and both men and women express emotion.

A high masculinity value indicates that work is more important than family life, the strong are admired, very few women are involved in politics, and it is not acceptable for men to express emotions (Hofstede, 2011). According to the *t*-test conducted for masculinity, there is no significant difference between the means of countries using IFRS as issued by the IASB and countries using IFRS as adopted locally.

IMPLICATION

This study implies that culture affects the interpretation and implementation of accounting standards, specifically International Financial Reporting Standards. The independent samples *t*-test analyses indicated the possibility that two of Hofstede's cultural dimensions, power distance and individualism, influence a country's acceptance of IFRS as issued by the IASB. This implication is consistent with prior studies (Chand, Cummings, & Patel, 2012; Doupnik, 2003; Liao, Sellhor, & Skaife, 2012; Portz & Strong, 2014; Tsakumis, 2007) that have suggested a cultural impact on the acceptance and implementation of IFRS.

CONCLUSION

Previous research has employed Hofstede's cultural dimensions to study aspects of accounting and IFRS implementation (Borker, 2012; Borker, 2013; Cieslewicz, 2014; Nurunnabi, 2015). This study expressed several noteworthy outcomes. First, many countries have accepted IFRS to some degree since previous research was conducted. This study reflects those changes accordingly. Secondly, this study categorizes the countries by the degree to which they adopt IFRS—whether using the standards as issued by the IASB, or as adopted locally.

Finally, the objective of this research was to determine whether culture has an impact on a nation's acceptance of IFRS. Comparing the two groups of countries through independent *t*-tests, and by using Hofstede's cultural dimensions, this study found that countries using IFRS as issued by the IASB have a significantly higher mean value for power distance and individualism. The dimensions of uncertainty avoidance and masculinity were found to be insignificant.

This study presents an opportunity for future research. Hofstede, after identifying the original four cultural dimensions, subsequently introduced two others—long term orientation and indulgence. Although not included within the parameters of this study, additional research could be performed to analyze if these additional values impact a culture's acceptance of IFRS.

In addition, Hofstede's data includes cultural values for countries that were not included in this study. Other groups of countries that were not identified in this study could be analyzed in a similar manner. Further research could also apply Gray's (1988) hypotheses regarding the relationship between cultures and accounting systems. These hypotheses were based on Hofstede's cultural dimensions, from which Gray derived four accounting value dimensions.

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