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THE CLASSIFICATION OF INTERNATIONAL ACCOUNTING PRACTICE
(La classification des pratiques comptables internationales)

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INTRODUCTION

As long ago as 1844⁽¹⁾ an early comparison of international accounting practices was published and standards for such accounting were discussed at the International Congress of Accountants in 1904, 1929 & 1933. Attention in these early years was rather spasmodic and inconclusive. In 1966 Sir Henry (now Lord) Benson was elected as President of the Institute of Chartered Accountants in England and Wales with an expressed interest⁽²⁾ in relations between national professional accounting bodies and an intent to promote more intimate relations between his institute and those of Canada and the United States. From this grew the International Accounting Study Group. Papers by Seidler⁽³⁾ and Mueller⁽⁴⁾ published in 1967 might be seen as an academic parallel to Sir Henry's professional initiative. A combination of professional and academic interest - and a growing interest in accounting for multinational corporations has ensured that this impetus flourished.

The MNC's interest in international accounting may be assumed to lie in areas of consolidation, tax minimisation, raising capital in several countries and obtaining quotations in various stock exchanges making it essential that accountants in these organisations understand accounting requirements for many countries. Practising accountants carrying out audits of MNC's need similar expertise, and accounting academics naturally interest themselves in this widely-demanded aspect of accounting. Another, perhaps stronger, argument for academic interest in international accounting was given by Seidler who drew attention to the way practices of other countries can demonstrate to students the application of what are otherwise theoretical concepts.

There are many supporters for the use of standard accounting practices across national frontiers, but less agreement as to which practices are to be adopted. This may be because accounting practices in different countries result from differences in cultural environments and corporate objectives. In any case, even if such a universal standard could be found it can only be a long-term solution and there is a need for something on a much shorter time-scale. Therefore it is suggested there is a need for every country to promote an understanding of 'foreign' accounting principles. This would require every accountant to have an understanding of the accounting practices of every country with which is in contact.

Gaining this knowledge is almost impossible. Every country demands lengthy training for its 'own' accountants, and few will allow a 'foreign' accountant to practice without a rigorous test of local competence. Although this applies with less force in MNC's, it is reasonable to use this as a measure of relevant competence. Thus it would take most of an accountant's life to complete this 'basic training'. It is possible that a study, not of the detailed practices in each and every country, but of the way in which practices may be expected to differ in varying circumstances would be an adequate substitute, and allow the accountant to concentrate on areas of greater importance. Although this is not likely to be accepted in place of professional qualification it does give a better understanding and is a major reason classification of national practices.

In the period since Sir Henry drew attention to this international field five distinct classification methods have been suggested and although each differs from the rest, examination suggests an evolution towards what may be seen as the 'best' system.

EARLY CLASSIFICATIONS

Seidler⁽³⁾ and Mueller⁽⁴⁾ drew conclusions from their own observations and experience. Seidler was designing an accounting course for international business students and drew two quite separate conclusions. First that international variations in accounting gave practical examples of ideas that were considered in the USA at that time in theory only. Second that to study these differences there is need of a way of grouping the countries

and their practices so that the whole range could be studied systematically. It was the second conclusion that gave rise to his classification based on the existence of 'Mother Countries', whose accounting practices had been adopted by others in their 'Spheres of Influence'. These influences may be colonial, political, traditional, or geographic. The three 'Mother Country' models that Seidler identified and some examples of their spread are as follows:

1. The British influence on Australia and India that resulted from colonial influences generating practices that did not disappear with colonial status.
2. The American model, originally derived from Britain but now seen as being distinct and influencing Mexico as a result of geographical proximity, then "La Mexico" as a 'conduit' into much of South America. It was also adopted voluntarily by Israel, and by Japan as a result of conquest in World War II.
3. The Continental (primarily French) model covering most of Southern Europe and the Mediterranean and is reflected in many South American countries embodying parts of the Code Napoleon.

Seidler says 'mother country' models are rarely perfectly reproduced and in many cases such as Canada, more than one sphere of influence overlap. He identifies other divergent forces: similarities between countries with similar legal systems (Common Law and Roman Law systems); effects in different countries of varying degrees of integration of tax and financial accounting; the influence of certain economic factors and differences in the perceived objectives of accounting. But the strongest 'message' from Seidler is that there is a need for classification of the ramifications of international accounting with grouping based on the similarities of practices.

Mueller⁽⁴⁾ used economic factors and offered four different approaches, these were:

1. The Macroeconomic Approach where the goal of the firm normally followed (rather than led) national economic policies although it was not necessarily an absolute condition since firms are part of the public interest that directs and influences national policies. This is typified by Sweden.
2. The Microeconomic Approach where the government trusts much of the nation's economic health to the activities of firms. This is said to lead, inter alia, to an emphasis on replacement value accounting, typified by the Netherlands.
3. The Independent Discipline Approach where the evolution of accounting results from its existing as a service to business independent of the economic constraints of the two preceding approaches, typified by the UK and the USA.
4. The Uniform Accounting Approach where the whole accounting activity (including the recording or book-keeping stage) is set in a uniform pattern throughout the country has the appeal to government of administrative convenience, assisting collection of economic statistics and aiding decision-making, and to the business community of convenience in application & use - especially when comparing one business with another. It flourishes in totalitarian regimes, was highly developed in Nazi Germany and imposed on many countries occupied during World War II. France is one that retained this after liberation. The Communist Bloc uses uniform accounting.

Mueller later extended this to ten groups⁽⁵⁾ but, as Nobes pointed out⁽⁶⁾, this method actually addresses, not the accounting, but its evolution. Seidler and Mueller may be seen as laying the foundation for future work although neither gave a satisfactory system since they lacked precision and mutual exclusivity between their groupings.

AAA INITIATIVE

The next landmark in the evolution was a report of the AAA Committee on International Accounting Operations and Education of 1975-1976⁽⁷⁾. This committee researched into the whole field of classification, concluding that the value of classification of accounting systems could be summarised into two distinct areas:

1. It sharpens description and analysis.

2. It has predictive powers in that:

- (a) One country imposing its system on another should be able to predict the probable development of the system.
- (b) Ontologically it should be able to predict the probable path of development of a country's system.
- (c) Linking accounting with politics and economics, would help predict how a change in one would affect the other(s).

To achieve this, classification should embody four attributes:

- 1. Consistency. Refers both to the need for adherence to the classifications set, and the need for the system to be consistent with its defined objectives.
- 2. Exhaustiveness. Classifications must cover the whole field of possibilities, but not merely by an indiscriminate increase in the number of classifications.
- 3. Mutual Exclusivity. Where levels are used each subclassification must clearly belong to one and only one superior group.

Having decided the attributes of a system to classify accounting practices, it suggests a morphological approach and illustrates a system covering six developing countries. The example actually demonstrates the major weakness of the system - if the morphology is to satisfy the need for adequate unique identification of each country's practices the resulting table is so large and complex as to discourage all but the most dedicated researcher. This may be solved with a computer, but that may distance the researcher from his data making it more difficult to conceptualise. There is also the risk, with any mathematical method, of the apparent accuracy obscuring the real meaning and reliability.

THE PRICE WATERHOUSE INTERNATIONAL (PWI) SURVEYS

In 1973⁽¹⁾, 1975⁽²⁾ and 1979⁽³⁾ PWI published world-wide surveys of accounting principles and reporting practices, all based on reports from their branch offices. The countries covered in these surveys varied from 38 to 46 to 64, and the propositions from 233 to 264 to 267. An independent survey was made by Dougnik and Taylor⁽⁴⁾ in 1983 attempting to extend the cover to a full decade. (This covered 50 countries and 76 propositions). A number of researchers used this detailed documentation as input for statistically based attempts to derive classifications. Before assessing these, let us consider some of the possible weaknesses of the survey data for this purpose:

- 1. Subjectivity must be expected in the responses.
- 2. Bias towards making the respondent country's practices seem more 'acceptable' is a possibility that cannot be dismissed.
- 3. Risk that the report may be a reflection of Price Waterhouse policy rather than typifying 'native' attitudes.
- 4. Personnel changes could mean succeeding questionnaires may have been completed for a country by different individuals.
- 5. Permitted responses changed from one survey to the next.
- 6. Brevity of Descriptions. In the 1979 foreword PWI state that these may mask important variations in a particular country, and cautions against drawing too precise an interpretation of specific matters or in relation to specific countries.
- 7. Interrelationship of propositions. The survey-reader is cautioned against interpreting the response to one proposition in isolation from others.
- 8. "Majority-of-a-Minority Situations". - E.g. "Jamaica and Zimbabwe show in tabulation 193 the predominant practice as to treat deferred taxes as assets or liabilities and adjust for changes in tax rates; but tabulations 189 and 190 show deferred tax accounting as a minority practice in these countries. The responses to 193 are therefore to be read in the context of 189 and 190; that is, of the minority who practice deferred tax accounting in the two countries, the majority treat deferred taxes as assets or liabilities and adjust for changes in tax rates." A number of such situations can be identified in the survey.

ATTEMPTS TO DERIVE CLASSIFICATIONS STATISTICALLY

Despite all these shortcomings, the Price Waterhouse Surveys are a heaven-sent store of detailed information and many researchers tried to derive classification groupings from it using mathematical or statistical methods. The more prominent of these being: In Costa, Bourgeois & Lawson⁽¹⁹⁷⁹⁾, Frank (1979)⁽¹⁹⁷⁹⁾, Nair and Frank (1980)⁽¹⁹⁸⁰⁾, Dougnik and Taylor (1984)⁽¹⁹⁸⁴⁾ and Goodrich (1982)⁽¹⁹⁸²⁾.

Each is different and deserves individual study, but space prevents this here. They can be considered together because of the common ground they share.

1. All use the Price Waterhouse Surveys as basic data.
2. All use statistical methods to produce groupings which they then justify by considering some national characteristics. (Generally socio-economic.)
3. All show a U.S. group and a British Commonwealth group among their final set but there is little other consensus as to the constitution of the groups.
4. All are affected by both the number of countries and of propositions covered.

Not only is there little consistency between different workers but even when the same worker moves from one survey to another. All these workers claim that use of a computer package guarantees objectivity: this may be true once the package has been selected and the input edited, but there is unavoidable subjectivity in the choice of package and in 'trimming' the data to match the input capacity of the package chosen. It may even be that this necessary subjectivity is a prime factor in the differences between results shown by different workers using the same basic data. These inconsistencies rather than the existence of subjectivity must invalidate any of the groupings thus produced.

It is clear, from the way groups change as countries are added, that these groupings are relative rather than absolute. Researchers claim changes of practice between surveys are responsible for the regroupings but, significantly, in no case is there a consistency of countries input. These researchers appear preoccupied with including all countries for which data are available regardless of consequence. The only researchers who set out to achieve consistency were Dougnik and Taylor, but even in their case the consistency was limited to the propositions and the number of countries was still allowed to fluctuate. As the AAA report concluded, classifications must be consistent and the indications are that classifications derived statistically are not consistent in the face of changes in size of population, and for this reason this approach must be discarded.

NOBES' JUDGEMENTAL APPROACH

Nobes' early work (1977)⁽¹⁹⁷⁷⁾ examined the development of accounting in Europe and identified a number of factors which he saw as influencing that development:

1. The legal system: Common Law and Roman Law having different influences.
2. Ownership Patterns: differentiating between countries where shares tend to be family-owned (France), controlled by banks (Germany), or held by a range of share holders (UK and USA). These influence presentation and contents of accounts.
3. The Accounting Profession develops differently in different countries, and the strength it attains also affects the accounting practices of that country.
4. The Size and Strength of the Capital market (both primary and secondary) can be seen as also influencing the preparation and presentation of accounts.

In later work^(1980, 1982) Nobes reviewed the whole subject. Agreeing with the AAA Report on reasons for, and desiderata of, such systems, he proposed the taxonomical approach of biology with hierarchies built up in levels, suggesting that social sciences show a vagueness and lack of formalised generally accepted theories compared with the physical sciences. He is concerned with the need to concentrate on the "essential structure" and avoid being "blinded and distracted by a mass of practical details". (A similar point is made by David and Brierley⁽¹⁹⁸¹⁾ when they divide laws and legal systems into 'families'. They insist on a need to differentiate between "constant elements" and less stable rules found in law at any given moment, asserting that no matter how important legal rules are they do not highlight the truly significant characteristics of a given legal system.)

Nobes concludes that a successful classification of accounting systems will be a hierarchical taxonomy relying on applied judgement based on detailed understanding of the countries classified. This requires knowledge of, not merely data about, the countries concerned. Nobes therefore restricted his classification to countries of which he had acquired the necessary breadth and depth of knowledge. His initial classification^[19] comprised "fourteen developed Western nations" selected for their influence and importance in seeking international harmonisation. Later^[20] this was extended to twenty countries and then to most of those covered by PWI in 1975, the omissions being due to lack of knowledge rather than any weakness of the system.

Bailey^[22, 23], a student of Russian accounting, used Nobes' methods to classify eleven communist countries. Consistency of methodology makes it possible to combine his work and Nobes' to produce one table (Table 1) covering 48 countries. It is important to note that (in contrast to the statistical models) the growth in the number of countries from 14 to 48 has involved no reclassification of any country. It has merely necessitated additions to the initial set of taxes (which is only to be expected).

Apart from the sequence outlined above, there seems to have been very little published work testing Nobes' hypothesis. This may mean that all who tested it found it stable, or that it has not been rigorously tested except by Nobes himself. Lacking evidence to the contrary, this paper assumes that the hypothesis has stood up to testing.

THE NEXT STEP?

Two parallel themes may be identified: (1) Classification can be seen as having evolved, from general statements intuitively based on incomplete data, an examination of classification itself, a detour into statistical methods, to a rigorously applied judgemental approach based on knowledge; (2) an increasing appreciation of the influences on accounting of environmental factors until, in Nobes' hypothesis, they become predominant.

What will be the next step in this evolution - or is there to be another step? Much work has been done in recent years by McComb^[24, 25], Hofstede^[26, 27, 28], and Gambling^[29, 30], on the interaction between culture and accounting. It is not clear yet whether this is the precursor of a new direction or if it will further confirm Nobes' hypothesis. If the former the evolutionary process may be said to be continuing, but if the latter there is a temptation to suggest that the 'ultimate' classification method has been identified and all that will follow will confirm and elaborate upon it. In which case, it only remains for the necessary knowledge to be acquired for the classification to be extended to cover all the countries in the world.

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