GLOBALISATION AND ITS IMPACT ON ACCOUNTING

Key words: Globalisation, accounting.

In this short research note, I first consider the origins of and define the concept of globalisation. It is contended that the impact of globalisation is increased policy homogenisation among countries. Then some features of the impact of globalisation on accounting are discussed. It is concluded that striking the right balance between effective participation in the processes of globalization and retaining of an accounting system that is useful and relevant to domestic needs is a very challenging task.

The implementation of the Marshall Plan to overcome political, economic and social problems of post-war West European societies and economies may have provided the trigger for the processes of «globalization». Globalisation has had the effect of making the world both larger smaller simultaneously. Global organisations are not citizens of just one country, but instead may both influence economic policies, and be influenced by, the legal and financial systems of the individual nation states in which they operate and to whose law they are subject.

Probable causes of globalisation are the removal of currency barriers, the elimination of «protective» import tariffs and the creation of regional trade zones to encourage foreign direct investment (FDI), globalisation of markets has occurred because of «the connection of national markets has come about through reductions of barriers to cross border trade investments»1. Industrial trading agreements were followed by political accords and national treaties leading to the formation of institutions such as the European Union (EU), International Monetary Fund (IMF), World Bank (WB), European Bank for Reconstruction and Development (EBRD), World Trade Organisation (WTO), etc. Under «the active patronage of such Western institutions»2, American and West European ideas, ideology and companies along with their products and services have crossed national
borders, spanning the globe. Coupled with the development of information technology, this has led to an increasing internationalisation of business and a worldwide integration of financial markets. As Qhmae explains it, globalisation is a process characterised by a free migration of information, physical and monetary capital as well as population.

The development of globalisation as a process has been accompanied by controversy amongst policy makers and academics. The practical implementation of the concept has led to problems such as, «should national economies be globalised?», or «what are the costs and benefits of economic globalisation?».

The financial markets illustrate some of the problems. The «domino effect» caused by the «Big Crash» of 1987 is a good example of the links between markets from New York to London and Tokyo. There proved to be no boundaries with regard to the quick diffusion of information. One could argue that the consequence of the crash was the subsequent financial crisis, while the conclusion drawn from the crash was that it proved that the linkage between national financial markets did exist. Conversely, the failure of Barings Bank did not generate a «domino effect». Maybe, it could also be argued that globalisation itself helped prevent another worldwide financial crash.

The «globalization» phenomenon is linked not only to markets but also to firms and their economic activities. A fewer number of larger firms now have a global «footprint», from manufacturing organizations like Daimler-Chrysler or Ford, the service sector (PricewaterhouseCoopers. HSBC) to information, communication technology and media companies (Microsoft, Cable and Wireless).

One impact of globalisation is the creation of a «single» market based economy which operates on the basis of a common set of rules imposed by leading institutions such as those previously mentioned. Such a set of rules, common to all those that applies, may be conceived in a way does not necessarily meet all the specific needs of those to whom it applies. The downside of having a single set of global rules is that it leads to a diminishing independence of those that are subject to such rules. The EU is one agent for such institutional isomorphism. Acceding countries must join the «acquis communautaire» (the body of legislation that candidate countries must accept on joining the EU). «The quasi federal system of the EU is most of the time a massive transfer platform from dominant countries ... to other countries», notes Claudio Radaelli.

Increasingly those subject to global rules have to accept the constraints imposed upon their independence. Small countries often «agree» to constraints imposed by economically stronger countries on their freedom to choose. Increasingly there is a tension between policy makers at the centre and national government regulation at the periphery – «state subsidiarity» has increasingly become a contentious issue. Multi-layered policies result in bureaucracy, uncertainty and conflict. State autonomy is diminished. Playing fields become uneven. But, as Hughes and Hughes have noted, «an important but neglected area of research is the policy architecture that encompasses institution building and economic activity. The EU accession process has revealed stark differences in economic performance between existing EU member states and their new partners from the CEE».

The application of accounting harmonization policies to Central and Eastern Europe exemplifies such differences.

With a diversity of cultural and economic traditions, accounting standards have been established separately in each country, making the implementation of globally standardised accounting procedures difficult to achieve. Despite the ongoing «globalization» of business, markets and services, harmonisation of accounting practices amongst individual countries is still a slow process.

Conversely, the growing activity of international accounting firms and multinational companies has led to the export of Western accounting practices to developing countries. This in turn creates a dilemma for practitioner and academics. Should developing countries
establish an accounting infrastructure to suit their own specific needs or import accounting systems used by developed countries, from different economic contexts? Different countries have pursued different approaches to solving this problem, which, re-emerged in Central and Eastern Europe in the 1990s. At one end of the spectrum, countries such as Slovenia adopted accounting standards similar to the British-American system of generally accepted accounting standards. On the other side, countries like Albania use a system of accounting based on the French general accounting plan.

The convergence of markets, firms and policies has resulted in a form of state «isomorphism» – a tendency for different national policies to become alike. Accepted accounting and auditing standards and practices are intended to facilitate the global businesses referred to previously. The rise to prominence of the financial sector has also highlighted the increasing need to standardise and harmonise accounting practices. The establishment of international accountancy bodies such as the International Accounting Standards Board (IASB) has served the above purpose. International trade, multinational industries and services, capital mobility and developing financial markets have significantly expanded investment opportunities. Accordingly, individual and institutional investors need to be able to read and analyse the language of domestic and foreign business entities in order to make informed investment decisions. Although accounting is the «lingua franca» of business, due to the fact that accounting standards and practices are separately established in each country, it is necessary to «translate» them into an easily understandable business lexicon. Accounting is however: «... a language for which there is no common grammar. Hence the anomaly that in a global economy, there is no globally consistent accounting language».

Further, as Raffournier and Walton emphasise, the importance of translation in the accounting process cannot be under-estimated: «Research by Choi and Levieh (1991) showed, by way of example, that 50% of investors interviewed in New York, London and Tokyo did not invest in foreign stocks largely as a result of not being able to analyse their accounts. The problem is experienced not only by investors but by companies wishing to attract investments...».

The rise to prominence of the financial sector has highlighted the increasing need to harmonise accounting practices. The European Union’s 4th Directive issued in 1978 was intended to harmonise national accounting policies with a comprehensive set of rules to be implemented by public and private companies in Europe. Although individual member states are permitted to derogate from the 4th Directive, it specifies:
- the format for balance sheets and profit and loss accounts;
- balance sheet disclosure requirements;
- valuation rules based on historical cost (the option of current cost treatment was advocated by UK standard bodies);
- the portrayal of a ‘true and fair’ view which prevails over domestic provisions in situations specified by individual member states.

The 4th Directive also laid down strict criteria on disclosure of items such as long term and secured debt, affiliate companies, director’s compensation, tax payable and tax charged to operations, as well as specifying the treatment for property, plant and equipment, intangible assets, inventories, liabilities, debt and inflation accounting.

The 4th Directive was followed by the 8th Directive, which specifies the qualifications necessary for professionals authorised to conduct statutory audits, but did not deal with mutual recognition issues, or the professional independence requirements for auditors, which still varies amongst EU countries.

This prompted the then Head of Financial Information Accounting Standards at the European Commission to comment: «It must be admitted that the comparability achieved through the harmonisation process is far from perfect. The accounting rules contain primarily minimum rules. They are not dealing with a number of important issues. Secondly they are not all interpreted the same way by member states».
The programme of harmonisation has continued to evolve, but the question remains «how to harmonise?» In May 2000, the European Commission drafted a new regulation requiring all EU listed companies to prepare accounts in accordance with International Accounting Standards (IAS) by 2005. This is the EU’s most significant action aimed at enhancing the comparability of financial reporting since the 4th and 7th and 8th Directives, and is intended to promote an integrated European capital market, in which high quality transparent and reliable financial reporting are paramount. Nevertheless, this has already caused controversy in Great Britain, where financial statements are prepared under the UK GAAP. In addition, the problem of how to reform and harmonise accounting practices in some Central and East European countries still remains. One of the main difficulties is that international accounting and financial reporting standards are subject to continuous updates and/or changes, and that global best accounting practices themselves are a moving target and require constant monitoring and regulatory and structural adjustments. Furthermore, the international accounting standards have aimed primarily at large, publicly quoted companies many of which also tend to be multinational in nature.

Past and current developments as well as future trends, assert that as a result of