

## Assessing International Accounting Harmonization Using Izomorfism

**Erdal YILMAZ**

19 Mayıs University

Finance And Account Lecturer

[erdalyilmaz1971@hotmail.com](mailto:erdalyilmaz1971@hotmail.com)

**Okan GELMEDI**

Sakarya Univeristy

Finance And Account Ph.D. Student

[okangelmedi@hotmail.com](mailto:okangelmedi@hotmail.com)

**Abstract:**The purpose of this study is to tell the convergence process which is being tried to be created by using the izomorfism concept with the standards of international accounting and financial reporting about accounting records and financial reporting throughout the country. Convergence is the activity in which accounting and related sections work together with the purpose of contributing to the development of a team of accounting standards for every country to be able to use them globally. However, in the studies done in this concept direction it is seen that, by ignoring the differences between countries and the negativenesses resulted form county dynamics, these studies gradually turn into the shape of an obligatory izomorfism. Obligatory izomorfism concerns the way in which organizations are subject to external pressure, either from organizations they depend upon, or from more general cultural expectations. We think that , as a result of these applications, in the future the regulations that each country will form by adding their own dynamics will come out and the applications will be similar, not the same.

**Key Words:** Harmonization, Accounting Standards, Financial Reporting, İzomorfism

### Introduction

Particularly the acceleration of mutual business traffic worldwide and the intention of businesses to operate in countries other than where they are based made it compulsory for all countries to develop a common accounting language. This is why the convergence efforts, which are described as the identification of accounting practices or *the collaboration efforts of accounting-related organizations with the aim of developing new standards that will contribute in creating a set of uniform accounting standards that every country can use on a world scale*, have started. To achieve this, accounting committees formed worldwide started publishing International Financial Reporting Standards (IFRS). As the national legislation should support the published standards in order that they can be implemented, they are adopted as national standards by countries. However, cultural differences between various countries have rendered the standard application goal of the standards inaccessible.

### The Study

With the increase in international investment activities and rapid circulation of capital globally, global economy gained an important acceleration on the one hand while the capital holders started enjoying higher profitability on the other. Firms bound to the international market with an expectation of better profits are bearing the costs largely while making investment decisions. Particularly because the financial indicators relating to the investment area or financial statements of companies are prepared based on varying accounting systems and practices in individual countries, investors were required to bear significant costs during the decision-making process and make various conversions in order to test the accuracy of such financial data and render them understandable for themselves. One of the efforts conducted aimed at reducing said costs of investors are the efforts to narrow the differences in the accounting systems of individual countries. This is because the losses and costs borne by global capital holders for their decisions in the countries they invest in made the accuracy of financial statements in invested countries questionable. ( Gönen,Uğurgel:p.1) This is why convergence efforts have started today as a non-returnable development process. (Moussa,2010;p.1) IASB, FASB, and other standard-setting organizations describe the concept

of convergence as increasing the conformity of the standards of each organization for high quality financial statements. To ensure this standardization, these organizations set and publish accounting standards, and the countries adopt these standards sometimes with minor changes but as a national accounting standard most of the time. That is, the intent, which was the convergence, meaning quality financial reporting, has become uniformization aiming to comply fully with the standards published.

However, the evolution of standards in the form of uniformization gradually puts accounting practices away from the socio-economic realities of the country. To illustrate; while business transactions in certain countries are made beforehand, they are mostly done at fixed future times in countries like Turkey. In which case, the impacts of accounting standards regarding the recognition of term differences shall vary from one country to the other. Moreover, many problems are encountered during the stage of application of standards. This is because accounting practices have become different in all countries for different reasons.

The main reasons underlying the differences in the accounting systems of countries are listed below:

- Legal System**
- Sources of Finance**
- Political and Economic Development**
- Economic Crises**
- Taxation**
- Securities Exchange**
- National Culture**
- Inflation**
- Reconciliation of Accountants**

Demanding that accounting practices become completely the same and trying to pump an excessive optimism is a vain effort in the face of existence of many differences caused by the above reasons in the accounting systems and practices worldwide. Even though a uniform accounting system is achieved as a result of efforts shown for the standardization of these efforts, the outcomes might not be as desired. This is because the interpretation and application of standards by countries with differing accounting cultures will naturally vary.

Despite this fact, the convergence efforts conducted so far bear a continuous quest for uniformization. Uniformity is full compliance with a structure or rule. Uniformity aims to realize international accounting as a uniform purpose at the conceptual level and practical level. (Çankaya, Aydoğan, 2008, p.302)

It may be remarkable to see the standards adopted by many countries despite the presence of so many reasons. However, the question we should ask is: Is convergence a practice that countries are willingly into? Or have the countries really adopted the standards in consideration of the positive effects of accounting standards on accounting practices? For us, convergence is essentially a uniformity imposition of global conditions in its current practice. At this point, we see this imposition as compulsory isomorphism. Isomorphism, meaning identity of form, means the organizations working in the same framework having identical conditions and resulting in the formation of similar structure and actions, and making similar arrangements as a result of similar restrictions.

However, in compulsory isomorphism, organizations are pressurized by external pressures, general (cultural) expectations, and other organizations. "From this point of view, adoption of international accounting standards emerging within the frame of convergence efforts as a whole by many countries may also be considered compulsory isomorphism." (Rodrigues, Craig: 2007, p.743) For example, the reasons underlying the adoption in Turkey as a whole of international standards published by standard-setting organizations (its creating isomorphic conditions by necessity) are as follows:

**1-Globalization:** Currently puts Turkey as well as the entire world into type concept of convergence.

**2-EU Negotiations:** While chapters are opened and closed in The process of Turkey's accession of the EU, the standards are accepted with the thought that it will result is support as there is a desire to ensure harmony with Europe on all matters in Turkey.

**3-Desire to Increase Foreign Investment:** Because Turkey is a developing country, there is a desire for increasing the capital build-up in the country and ensuring economic enhancement. Standards are being adopted to facilitate the procedures of capital holders that will invest in Turkey, and to assist in evaluating the companies they will buy, and this will is reflected in the Turkish Commerce Code currently being discussed by the Turkish Grand National Assembly.

**4-Pressures from the Business World:** Turkish business world asks the adoption of standards on grounds that it trades and collaborates most with the European countries

With these and such other reasons, many countries are adopting the international standards "by necessity" as their national standards. For example, the desire to increase foreign investment is a desire of not only Turkey but of other developing countries as well. On the other hand, all countries desirous of attracting foreign investments try

to see the *same* capital holders in their countries. That is, as in the definition of isomorphism, developing countries are aiming the same capital, and as can be easily imagined, that the other developing countries take measures aiming to reduce the costs and increase the trusts of such capital holders and, for example their adoption of international standards, putting Turkey into an isomorphic practice and resulting in the Turkish translation of the international standard and its publishing as a national standard. When doing this, general expectations are pressurized and led by the business world and capital holders. This shows the necessity dimension of the isomorphic practice.

### **Problems Of Convergence And Proposal For Solution:**

The process of convergence continues in the entire world with various problems. The main problems of the process are mainly as follows:

- (1) Problems on interpretation,
- (2) Language related problems,
- (3) Problems on technical terminology (terminology problem)
- (4) Problems relating to changes in profit measurements,
- (5) The role of capital markets,
- (6) Political influences.(Demir,2009,p.5)

With IFRS's published in the convergence process, the aim is to increase liquidity, level of transparency, international collaborations and fund collection abilities from international markets, reducing funding costs, preservation of competition and contributing to the efforts aimed at creating an economic union. Standards to serve this aim should offer principle-based, dynamic, abstract-priority dependent solutions, suitable for all conditions and businesses. (Gönen, Uğurgel, p.1) However, as mentioned above, there are many problems preventing the formation of standards with such principles. For example, the understanding and desire that the standards should be principle-based does not match Turkey's accounting structure. Turkish accounting system has a tax-based approach, the legislator prepared its accounting regulations on tax basis and principle-based in parallel with this. However, as mentioned above, expectations and coercions have put Turkey in a position to develop isomorphic practices for principle-based standards.

In fact, uniformity is the adoption of all other countries the accounting practice and reporting standards of several countries. Today, considering the economic effectiveness of capital-intensive countries, if we assume that capital-intensive -developed- countries will be more effective in these accounting practices and reporting, that is if we accept the standards as a common language, it is obvious that developed countries will inject more words into this language. It is clear that developing countries will use the language of the developed ones if the language develops in this manner. Just as a human being speaks his own language best, it should be able to arrange its financial reports first based on the needs of its own country.

Speaking the uniformizing accounting language "by necessity", and creating isomorphic practices, developing countries are negatively affected by this process. A situation might arise resembling the difficulty of someone speaking another language in his own country. This is because the developed countries where there are more capital holders have become an industrialized, professional and an informal society. Capital-holding countries mostly look alike one another. For example, an accounting convergence between Germany and France might not be rejected by both of these countries. However, trying to uniformize the accounting practices of Germany and Turkey will create different responses, also bringing many challenges. The economic structure of countries, and their above-mentioned cultural differences will make it difficult to practice the same accounting system. For example, level of avoidance of uncertainties, one of Hofstede's cultural dimensions, is lower in countries with higher capital accumulations, which will make it easier to adopt new standards, as they are bolder and have risk-based understandings. So the best thing to do is to make efforts in order to minimize the differences between practices and systems.

If the aim of convergence is to create a common language in accounting practices and financial tables and to speak that language, the only way to create a common language cannot be the convergence process aiming uniformization.

In its place, ways should be considered that would minimize the differences among countries. Mutual recognition and reconciliation are some of the alternatives we can mention at this point.

Mutual recognition expresses the acceptance of national financial reports although they are not prepared according to the accounting principles of foreign countries. Mutual recognition is in practice between USA and Canada. US companies may be traded in the Canadian Securities Exchange with US-GAAP'-compliant financial statements. American companies can trade in the Securities Exchanges of European Union countries based on financial statements prepared in compliance with US-GAAP. Although mutual recognition is very well practiced in

the case of Canada and the USA, the role of close economic and cultural ties between the two nations and the identity of standards and targets in accounting should not be forgotten.

Reconciliation is the permission for preparation of financial reports of foreign companies according to the accounting principles of their countries. However, in reconciliation, reconciliation is established arrangements relating to net profit and equities, which are considered as the most important factor by users of financial statements. The purpose of reconciliation is to reveal the great differences arising between the accounting practices. Thanks to reconciliation, foreign investor companies can obtain information about their assets and profitability levels based on their own accounting principles. As a result of the reconciliation, investors can make easy comparisons. The positive side of reconciliation is that it is less costly than the harmonization of all financial reports based on foreign accounting principles. (Çankaya,Aydoğan, 2008,p.307-308)

The concepts of reconciliation and mutual recognition also have negative aspects. The negative aspect of reconciliation are expressed to be its presentation of summary information relating to the financial situations of companies and its failure to make disclosures about the general conditions of companies. The negative aspect of mutual recognition is the difficulty that financial users might encounter in understanding different accounting standards. In fact, to remove such negative aspects, XBRL (eXtensible Business Reporting Language), supported for convergence, may be used. As the language of financial reporting, XBRL is a standard, platform-independent, digital data coding language to be jointly used by financial information producers and information users for data exchange. With this data coding language, businesses shall create their financial reports once and these reports shall require no rearrangement or conversion when transferred to other environments. It will be possible to use these XBRL-prepared financial reports for all financial report exchanges. XBRL permits coding any information about the business. So, loading information suitable for each financial statement item, financial statements complying with both international standards and national standards may be produced.

Harmonization efforts in preparing financial statements should methodically reduce the difference between accounting practices and increase the comparability of financial statements prepared and practices in various countries. This will also contribute en reducing the overall difference between the countries.

When the overall difference is reduced, problems in preparing and reading financial reports will also lessen.

## Conclusion

Globalization is an inevitable reality directly affecting today's economic, social and political events. With globalization, capital movements went beyond national borders, continuously searching for and utilizing new investment opportunities in the international arena. That the accounting system is based on different principles and rules in each individual country produced difficulties in mating rational investment decisions. As a result, there has been the necessity for common financial reporting system valid in all countries and convergence efforts continued led by certain countries and organizations. Every country's accounting system differs based on factors like their social, political, financial, cultural etc. environment. Set of uniform financial reporting principles to be imposed disregarding these factors shall not give the intended outcome, with many countries being obliged to produce and bear the costs of financial tables not directly addressing their specific needs, as a price of attracting investments to a country. Instead, unnecessary differences between the accounting systems of countries can be removed, while other differences are being made identical by mutual recognition and reconciliation. With the appropriate use of solutions like XBRL, which has emerged with technological improvements, both the needs of international capital and countries intending to maintain their national accounting systems will be greatly met.

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