Accounting Practices of Multinational Companies

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Abstract

This paper aims to review the available literature on the accounting practices of multinational companies. In order to do this, open-source articles from Google Scholar were used. An attempt was made to select studies spanning several decades so as to analyse the trends in accounting practices over the years and especially following increased globalisation of economies across the world. Using specific criteria, approximately 500 scholarly works were initially analysed and then reduced to a smaller number which were then explored in detail. It was found that in the case of multinational companies, accounting practices have had to adapt to local norms and cultures. National economic, social, political, cultural and legal considerations make it difficult for the adoption of a universal and global accounting system that would impose standardisation and ensure uniformity across multinational companies. The push, therefore, has been in favour of harmonisation, which has allowed for flexibility as well as uniformity. This has been met with success as compared to previous attempts at global standardisation.

Keywords: Accounting, international accounting, accounting practices, multinational companies, standards in accounting, harmonisation

Introduction

Accounting is often understood as pertaining to the measurement and processing of financial and non-financial information. This field has undergone several changes over the years. Accounting may also be used to provide pertinent information relevant to the decision-making practices of businesses. Therefore, accounting may be understood as a way to communicate an organisations finances to multiple stakeholders such as the company's managers, banks and governments. Accounting in multinational companies had existed since the time of imperialism when it was mostly restricted to book-keeping activities and tax collection schemes (Choi & Meek, 2011). With globalisation, however, the field has needed to adapt to the increasing demands that come with expanding to other countries and incorporating diversity while also maintaining certain standards across the board, combined with an increased level of accountability and scrutiny. In addition to this, multinational companies may be understood as 'a form of collection of autonomous operating units under a distant control' (Saidu & Ahmad, 2015:1312). These companies often refer to 'a relationship similar to the parent and subsidiary form in which the parent company operates beyond the shores of the home country through affiliates in another country' (Saidu & Ahmad, 2015:1312). Hence, multinational companies are those wherein the parent company and its subsidiaries are based in different countries and will, therefore, have accounting practices across the various countries that they operate in. Accounting practices in multinational companies can be varied and include Foreign Direct Investments, international taxation, foreign currency translations for balance sheets, as well as conducting audits (Saidu & Ahmad, 2015).

Accounting practices are, state Radebaugh, Gary and Black (2006) influenced not only by the company but also by the country that the company is based in. This is because a country's political system, its culture, its taxation laws and economic considerations such as inflation, inform the accounting norms. Hence, the accounting practices of multinational companies can vary greatly, depending upon the country the company is based. This diversity has meant that the field has had to adapt and develop context-specific guidelines where ever required. This has meant maintaining a balance between adaptation, flexibility and uniformity, which is required from the various branches of the same company across the world. At the same time, attempts have also been at global standardisation, which will be discussed further in the Results section, in some ways the field has had to restrict and adapt itself to adhering to local norms and practices.

In the following sections, the search conducted will be explained, followed by the findings of the review and what the various studies reveal about the accounting practices of multinational companies. This will be followed by a conclusion that will sum up the arguments and discuss the scope for future interventions and research.

Methodology

In order to find relevant research studies, specific terms were used in Google Scholar. These were the following: accounting practices, accounting practices & multinational companies, accounting & multinational corporations, international accounting, and international standards accounting.

For each individual search term, 100 results were considered, for a total of 500 results. For these, an initial examination was conducted, using research studies that spanned several decades, while special attention was paid to those after the 1980s and 1990s. This was based on the assumption that accounting practices would evolve and face new challenges with increased globalisation. Hence, there was an attempt made at understanding the evolution of this field across several decades and especially in the context of increased globalisation.

Results

With increased globalisation and the expansion of international businesses, accounting too has had to adapt as a field, to the challenges presented. Schoenfeld (1969) states that all companies, regardless of their size, would face difficulties in their accounting practices while expanding and establishing themselves in other countries. These difficulties would arise, it is argued, due to a lack of ‘internationally accepted accounting principles’ (Schoenfeld, 1969:3). Perhaps the most important reason for standardisation, however, is that it would allow for comparative analysis between multiple branches of the same company. Therefore, the lack of standards is one of the biggest problems that multinational companies are faced with (Schoenfeld, 1969). It should be reiterated, however, that while standardisations would bring about an ease in accounting across countries, Schoenfeld (1969) along with Radebaugh, Gary and Black (2006) emphasise the influence that a country’s ‘legal, tax, economic and educational systems’ have on this field, resulting in ‘complex adaptations’ requiring ‘considerable time’ (Schoenfeld 1969:3).

In addition to this, Grey, Shaw and McSweeney (1981) raise fundamental questions while studying the need for standards in accounting, which include - ‘what should be required by the standards? Who should set the standards?’ (Grey, Shaw & McSweeney, 1981:121). The second question is especially crucial as it brings to focus the detriment that could potentially be caused by enforcing standards that are not context specific onto a country where they do not adhere to the existing political, economic and cultural landscape. Therefore the question that arises is - should the country of the parent company decide the norms and standards or the country where the subsidiary is based? Other concerns about standardisation have also included apprehensions about standards' ability to be flexible enough to adapt to the countries and cultures they are applied to (Choi & Meek, 2011).

Walton, Heller and Raffournier (2003) state that while keeping in mind cross country differences, there are two terms used in accounting that have often been used in order to find solutions - harmonisation and standardisation. While the former is used 'to mean the reducing of differences in reporting between countries', the latter has to do with 'the application of exactly the same rules' (Walton, Heller & Raffournier, 2003:9). Understanding this distinction is crucial, they argue, because while standardisation would negate the importance of country-specific influence on accounting, harmonisation would mean closing the gap between the differences, as best possible (Walton, Heller & Raffournier 2003:9).

In order to address these concerns, efforts at standardisation were made as early as in the 1960s with the Accounting Principles Board of the American Institute of Certified Public Accountants seeking to lay the foundations for a framework that would guide uniformity across accounting in multinational companies. This was followed by the International Accounting Standards Committee (IASC) which was set up in 1973 and then succeeded by the International Accounting Standards Board or IASB in the early 2000s. This body set benchmarks which could be used as guidelines in a standard set by companies in different countries. Hence, the process of harmonisation and standardisation began in the 1960s and laid the foundation for the later work done by the IASB. In addition to this, the United Nations (UN) and the Organisation for Economic Co-operation and Development (OECD) have also made attempts at streamlining processes and developing standards for multinational corporations. However, it is argued that such multinational organisations do not possess the implementing authority for imposing such standards, nor would such standards be effective if only applied at the regional level (such as only among OECD countries) and not accepted at the national level (Grey, Shaw & McSweeney, 1981). Hence, accounting practices of such companies need to adhere to the local needs and norms as well as with the international standards set by bodies such as the IASB. The default, therefore, tends to be the acceptance of GAAPs, or Generally Accepted Accounting Principles. These Principles aim at ensuring that there is some uniformity in a company's revenue recognition, balance sheet classification, etc. despite operating in multiple countries. Therefore, while there is an attempt at standardisation, this is only with regard to certain aspects that would need to be compared across countries (Deming, 2006).

The year 2005 probably marked the most significant development with regard to changes in the field of accounting when it comes to multinational companies. This is because, in 2005, international accounting standards started being used in a widespread manner. The year saw the introduction and subsequent adoption of 'global and high quality accounting standards' (Fleck & Cearns, 2008:501). This was a culmination of the efforts put in by the IASC and IASB, resulting in the International Financial Reporting Standards (IFRS). This marked the shift away from the acceptance of GAAPs towards the most uniform principles of accounting that have existed across multinational companies. Hence, with the adoption of IFRS, there is a demarcation in the accounting practices of multinational companies- pre-2005 and post-2005 and a move towards adopting internationally set and accepted standards.

Discussion and Conclusion

The results so far have highlighted the challenges that arise with the expansion of commerce and setting up of multinational companies across the world. It has also been highlighted that although having a uniform set of norms applicable to accounting would be beneficial and would facilitate the functioning of accounting practices in companies with ease, it too is not without its share of issues. While attempts were made over the past several decades to bring about a level of uniformity across the field, none had been very successful. This was due to a host of reasons such as questioning a company's ability to impose accounting practices onto a country regardless of its own culture as well as a lack of consensus on what the uniform standards should aim for. In 2005, however, a landmark was reached in the adoption of the IFRS. Although adopted by approximately 100 countries, this is still a landmark. This is because no other framework has had such wide acceptance in the past. A decade after its adoption, there have been avenues and opportunities for reviewing the effectiveness of these standards. In an attempt to evaluate the implementation of the IFRS, Ball (2016) states that one of the key highlights of the Standards has been that they were, 'designed to increase financial reporting transparency, which can be interpreted loosely as providing more complete and accurate information about the company's financial affairs' (Ball, 2016:548). Additionally, despite its widespread adoption, one must 'expect substantial variation across jurisdictions' and uneven implementation across countries (Ball, 2016:548). This is because no two companies are identical, and this is especially the case with multinational companies. An example of this may be seen in the case of Australia. Although the country has adopted the IFRS as the default standards, the country has made them restrictive, by removing certain choices and options (Fleck & Cearns, 2008). Hence, this is where the issue of context-specific implementation arises once again. Despite having adopted the IFRS, its implementation and consistency of implementation cannot be guaranteed. However, the IFRS does have benefits as well. Ball (2006) states that they utilise fair value accounting measurements' while also providing 'borrowers with choice among accounting methods' and 'providing fewer implementation rules and accordingly giving managers wider discretion in implementation' (Ball, 2016:560). It has been argued that the adoption of the IFRS has also ensured an 'enhanced comparability and improvement in (the) quality of financial information' and an 'increased reliability owing to narrowing the information gap between capital providers and individuals' who have been entrusted with their money (United Nations Conference on Trade and Development, 2019:2). Therefore, using the distinction made by Walton, Heller and Raffournier (2003), it may be said that while standardisation of accounting practices in multinational companies has not succeeded, strides have been made in moving towards harmonisation of these practices.

It is useful to mention here that one of the key reasons for the relative success of the IFRS is that the IASB enjoyed a certain level of legitimacy and was accepted as the standards authority. This is especially the case in the European Union and has paved the way for consistency of the IFRS and its implementation (Fleck & Cearns, 2008).

It is evident from the review that even though there has been unprecedented globalisation and expansion of markets in the decades since multinational companies and accounting first came to be, in some ways the practices have remained local. International accounting practices have undergone numerous changes in these decades and have had to adapt to the local economic, political, legal and cultural frameworks. Hence, there has been a need for global standardisation in order to bring about uniformity in the practices of this field. However, despite such attempts, implementation has still remained reliant on local factors, leading the way instead, for harmonisation of accounting practices of multinational companies. Harmonisation has seen relative success as opposed to global standardisation because it does not mandate a strict imposition of rules regardless of context. Sawani contends that harmonisation ‘does not force the elimination of national standards, which could be met with significant nationalistic opposition’ (Sawani:6). Therefore, harmonisation has allowed for comparability of international accounting data and information gathered across the various branches of a multinational company.

The review thus far has provided an overview of international accounting practices and the need for adaptation, flexibility and uniformity in the field. This has especially been the case when accounting practices are applied to multinational companies that require information across similar parameters from the various branches of the same company across the world (Sawani). This led to the demand for establishing standards that may be applied to accounting practices uniformly. Standardisation attempts were seen over the decades first through the setting up of the IASC in 1973, followed by the IASB in the early 2000s and finally the adoption of the IFRS in 2005. This evolution and subsequent success of the IFRS has shown that harmonisation rather than global standardisation is required in international accounting practices. This is because while a need is seen for standards and uniformity, this cannot be enforced upon a country, devoid of its cultural, economic, social and political context. As seen in the case of Australia, the IFRS has provided opportunities for adapting the standards to suit a country’s context and needs. It is this flexibility in international accounting that will pave the way for successful standards across multinational companies (Sawani).

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