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The Effect of Culture on the Implementation of International Financial Reporting Standards

Mitchell A. Skotarczyk
Claremont McKenna College

CLAREMONT McKENNA COLLEGE

THE EFFECT OF CULTURE ON THE IMPLEMENTATION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS

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PROFESSOR MARC MASSOUD

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DEAN GREGORY HESS

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MITCHELL SKOTARCZYK

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I. Introduction

As globalization increases at a blistering pace, more and more business entities continue to get involved in cross-border capital investments. A considerable cost can be applied to these types of transaction for the translation of financial statements prepared under dissimilar accounting guidelines into a comparable form. There exist a multiple number of accounting systems that create these dissimilarities, because accounting is a language of business that has been created by society to provide information as to the economic health of an entity. Similar to any other language, varying types of “accounting language” are used across different regions of the globe to convey this information.

The increased frequency of the resulting costs has created a demand for an internationally comparable set of accounting standards. The creation of the International Financial Reporting Standards (IFRS) has tried to fulfill this demand. The desire to have comparable standards has thus resulted in the adoption and implementation of, as well as the convergence to IFRS. Despite the push towards convergence of these accounting standards, significant diversity still remains.

The resulting discussions on how to achieve worldwide accounting convergence oftentimes only involve the differences between specific accounting standards and how to eliminate them. However, in order to know how to eliminate differences one must first fully understand why they occur. One major reason for these differences is culture. Unfortunately, the role of culture is frequently absent from this discussion, regardless of the fact that it is at the heart of many differences that exist between one accounting system and the next.

For this context culture can be thought of as the collective values of a society that influence its behavior. It is no secret that significant differences in these values exist internationally, and that these differences have a profound effect on all elements of society.

Therefore, accounting, as a societal creation, is influenced by these values as well. Given the goal of internationally adoption and comparability, it is important to explore the effect that culture can have on the implementation of IFRS and the challenges it presents to adoption. Through an examination of IFRS, aspects of its implementation, and the difficulties it faces because of culture, this paper proposes that IFRS will not be able to attain its goal of international adoption and comparability any time in the near future.

II. Literature Review

The effect of culture on international accounting standards cannot be examined without some sort of framework in which accounting and social values can be connected. The formation of this framework begins with the cross-cultural study of Geert Hofstede (1980; 1983). Hofstede's study attempted to identify important aspects of culture that had an effect on people's behavior in a professional capacity. This was done through a survey of people's values across 50 different countries and three regions. Values were analyzed on the collective level, and therefore, were thought to be the best representation of a country's culture.

From this survey Hofstede was able to draw out four dimensions of culture, which included: power distance, uncertainty avoidance, individualism, and masculinity. Power distance was thought to capture the extent to which there was equality in power between members in society. For example, in a society where there is great power distance, many individuals accept the authority and have no say in decisions that are made. Power distances attempts to most closely address, "how a society handles equalities among people when they occur" (Hofstede 1984).

Uncertainty avoidance involves the aversion one feels towards the unknown and what actions are taken as a result of that aversion. Those with strong uncertainty avoidance look to plan every detail without any room for flexibility or innovation. If a person has weak uncertainty avoidance then they will be content with letting things happen as they may. Uncertainty avoidance looks at whether a society, "tries to control the future or let it happen" (Hofstede 1984).

Individualism is a measure of whether someone feels as though they must fend for themselves or that they are a piece of a greater whole that will take care of them. Simply put, this, "relates to people's self-concept: 'I' or 'we'" (Hofstede 1984).

Finally, masculinity refers to a society's partiality towards, "achievement, heroism, assertiveness, and material success" (Hofstede 1984). On the opposite end of this spectrum is a society with goals rooted in relationships and quality of life, which Hofstede refers to as feminine.

These four values were later validated through a comparison with the Rokeach Value Survey (RVS). The RVS was first used in the United States to measure the importance of a set of 36 values. These values were then divided into two categories, with one labeled "terminal" and the other defined as "instrumental". In this model, terminal values refer to the desired outcome, whereas instrumental values capture the means to the outcome. While originally designed for use in the United States, the RVS was adopted for use in several Asian Pacific regions, including: Australia; Bangladesh; Hong Kong; India; Malaysia; New Zealand; Papua New Guinea; Japan; and Taiwan. Of the regions where the RVS had been performed, Hofstede had comparable data for all but Malaysia, Bangladesh, and Papua New Guinea.

Hofstede and Bond (1984) were able to examine the six areas were the RVS and the cross-cultural study overlapped. They indicated that in these areas there were significant correlations between the RVS variables and Hofstede's four dimensions. For example, the RVS values of obedient, polite, ambitious, and national security all showed a significant and high positive correlation with power distance. Through this process Hofstede and Bond were able to validate for the four culture dimensions with another measure of values. Hofstede's cross-cultural study provides evidence for the idea that cultural values differ on a measureable level across nations. This allows for a discussion of how individual societies' values vary and the consequences that holds for implementing rules on an internationally level, such as IFRS. In addition, the establishment of the four cultural dimensions laid the groundwork for incorporating culture into an analysis of the development of international accounting standards.

Only a few years later, Sidney Gray (1988) was able to use the four dimensions to create a framework that could be used to analyze the effect of culture on accounting systems. Gray recognized that the four dimensions of culture must somehow be related to the values in the subculture of accounting systems. He, therefore, proposed a link between the two by outlining the important values of accounting subculture while showing each one's connection to societal values. Gray proposed four main accounting values: professionalism versus statutory control; uniformity versus flexibility; conservatism versus optimism; and secrecy versus transparency.

Professionalism versus statutory control is meant to be a measure of the extent to which accountants have control over setting their standards. Accounting systems with a high level of professionalism have private standard setting bodies as opposed to public regulations. Gray proposed that professionalism could be most closely linked with both individualism and uncertainty avoidance. He then hypothesized that, "The higher a country ranks in terms of individualism and the lower it ranks in terms of uncertainty avoidance and power distance then the more likely it is to rank highly in terms of professionalism" (Gray 1988).

The second measure of accounting values, uniformity versus flexibility, looks to gauge the degree to which there must be comparability across time, reporting entities, or countries. For instance, a highly flexible system would allow for different accounting practices to be used to best suit the situation. Gray posited that uniformity could be linked to high uncertainty avoidance and power distance and low individualism.

Conservatism versus optimism addresses the degree of conservatism used in asset measurement and income reporting. This is regarded as an important aspect of accounting systems, and the connection with Hofstede's dimension of uncertainty avoidance can be seen quite clearly. A high level of uncertainty avoidance results in a desire for smoothing out reported income and asset valuation, thus resulting in a higher level of conservatism. Gray also holds that there is a weak relation between conservatism and higher levels of individualism and masculinity.

The fourth and final classification of accounting values, secrecy versus transparency, involves the willingness of reporting entities to disclose information. Secrecy relates to all four of the dimensions in such a way that, "The higher a country ranks in terms of uncertainty avoidance and power distance and the lower it ranks in terms of individualism and masculinity then the more likely it is to rank highly in terms of secrecy" (Gray 1988).

After outlining the four accounting values that are linked to cultural dimensions, Gray continued by examining how the country classifications made by Hofstede would be grouped based on their accounting systems. In order to do this, the four accounting values were grouped into authority and its enforcement and measurement and disclosure. Authority consisted of professionalism and uniformity, while measurement and disclosure contained conservatism and secrecy. In both cases, Gray placed one value on a vertical axis and the other on a horizontal access and then plotted the country classifications on to that four part grid. When analyzing the groupings that occur on the grid representing authority and its enforcement, there is no strong collection of countries in any one quadrant. The grid representing measurement and disclosure, however, shows all country classifications in either the quadrant for conservatism and secrecy or transparency and optimism with Anglo, Nordic, and Asian colonial falling in the latter category and the rest residing in the former. This is logically sound, as philosophies on measurement and disclosure would naturally go hand and hand.

After theorizing the framework for analyzing the impact of culture on the development of accounting systems, Gray called for an expansion on his work. The accounting values needed to be operationalized and empirical studies performed on their relationship with Hofstede's cultural dimensions. While his work in 1988 did not include an empirical study, Gray provided and explanation for how culture and accounting are connected. This in turn allows one to explore not only differences in culture, but also to consider the effect of those differences on accounting.

The empirical studies that Gray called for have occurred, including a study performed by Sudarawan and Fogarty (1996). In their study, Sudarawan and Fogarty used Indonesia as a study of the hypothesized connection between Hofstede's cultural dimensions and Gray's accounting values. The two researches first began by operationalizing the accounting values in order to statistically compare them to Hofstede's suggested predictors for his cultural dimensions. This study chose to ignore Hofstede's fifth dimension of long-term orientation, which was added in 1991. The rationale for this exclusion was that Indonesian society did not necessarily consider the future more important than the present, and therefore made the fifth dimension irrelevant for the study.

The authors believed that professionalism could be adequately represented as the number of methods used in financial reporting that were not allowed by Indonesian accounting standards as well as the number of standards issued by the Association of Indonesian Accountants. As a proxy for uniformity they used the number of alternate methods sanctioned by Indonesian accounting standards and the number of accounting changes. The third value of conservatism was measured simply as the number of permitted accounting methods. Finally, secrecy was shown by the number of disclosures required in the income statement and balance sheet under Indonesian standards.

The conclusion of the study showed that the proxies used for all four accounting variables proved to be related to those used for the four cultural levels on a statistically significant level. While relationships existed in the data, some did not match what was theorized by Gray. In response to this, the authors cite the influence of managerial discretion as a serious complication to evaluating the effect of culture on accounting systems. Managerial discretion can have an effect on many measureable accounting decisions, but is company specific. Therefore, this discretion may not have been representative of the environmental influences that the authors were trying to measure.

While there were some anomalies in a few coefficients, a majority of the results validated Gray's theory about accounting values, at least in the context of Indonesia. For example, the hypothesis testing showed statistically significant positive relationships between uncertainty avoidance and uniformity and between individualism and professionalism.

The authors hold that the work of Gray can only be validated by the continued replication of studies like theirs onto different cultures and nations around the world. While this is true, their study does help to provide support for the idea that this framework can be used to analyze the impact of culture on a multinational level. With the partial validation of Gray's work with empirical evidence, one can study differences in culture and confidently apply them to variances in accounting systems such as IFRS.

III. IFRS

The origins of IFRS reside in the attempt to address the need for a common language in accounting. The first attempt to meet this demand can be seen in the creation of the Accountants International Study Group in 1967. This group was composed of members of the American Institute of Certified Public Accountants, the Canadian Institute of Chartered Accountants, and the Institute of Chartered Accountants of England and Wales. Members of this group worked together to study common topics in accounting that were relevant internationally, such as the study on inventory accounting practices in 1968 (ICAEW 2011).

In 1972, Sir Henry Benson proposed the creation of the IASC. The next year the IASC was formed and Benson was named its first Chairman. The Committee was a response to increasing reliance on capital from foreign jurisdictions. The absence of a single set of comparable standards created inefficiencies in capital markets worldwide. Therefore, the IASC's goal was international accounting harmonization. The Committee was composed of representatives from Australia, France, Canada, Germany, Japan, Mexico, Netherlands, UK, and the United States. The IASC Board responsible for creating standards originally began with nine members, on from each of the founding members. In 1975, the IASC issued its first International Accounting Standard (IAS).

In 1977, the International Federation of Accountants (IFAC) was created in attempt to continue work on creating accounting standards and promoting cooperation between many regulatory and accounting organizations. The IFAC and IASC issued several statements of their commitment to work together. In 1982, the IFAC discontinued its role as a standard setter and recognized the IASC as the international standard-setting body. At this time, the IFAC also took responsibility for appointing 13 of the then 17 board members of the IASC (IFAC 2011).

Throughout its existence, the IASC worked with many organizations and nations in its attempt to create useable IAS. Two examples include: a project that involved working with bank governors to examine financial reporting for banks; and a project in 1981 which worked with the Netherlands, UK, and US to study accounting for income taxes. The IASC also wanted its IAS to be of the highest quality. Therefore, in 1987, they launched a project aimed at improving standards and enhancing their comparability. This involved the revision of many IAS and making them more prescriptive. The project was complete in 1993 (IAS Plus 2011).

In an effort to gain legitimacy as the preeminent creator of high quality comparable international standards, the IASC sought the endorsement of the International Organization of Securities Commissions (IOSCO). The move towards endorsement was solidified through an agreement between the IOSCO and IASC in which the two organizations agreed on a set of "core standards" necessary for cross-border listings. The IOSCO agreed to endorse IAS as long as the "core standards" were completed. The agreed-upon standards were completed in 1998, and the IOSCO endorsed IAS as the appropriate standards to use in cross-border dealings (IAS Plus 2011). The endorsement of IOSCO carried with it an increase in responsibility for the IASC that the organization could not handle in its current state. Therefore, the IASC began making plans to reorganize.

The reorganization of the IASC into the IASB began with a strategy review performed by the IASC from 1997 to 1999. In 1997, the IASC created the Strategy Working Party (SWP) to explore possible options for the future of the IASC after they finished their "core standards". Their first step was release a discussion paper titled "Shaping the IASC for the Future". After issuing the paper, a joint meeting was held between the IASC and the SWP in which the new structure of the IASC was discussed.

The two parties came to the conclusion that the best structure for the IASC moving forward consisted of a single standard-setting board. The board would be made up of some full-time members and some part-time members. This was a change from the part-time members that had previously made up the IASC. In 1999, a proposed structure for the new IASC consisted of reorganizing the IASC as an independent foundation with a board that set standards and a group of trustees that was responsible for appointing board members, fundraising, and oversight. In 2000, a new constitution was approved which was based upon the proposed structure and called for 19 trustees and 14 board members. On March 8, 2001, the IASB was officially put into operation and began issuing new standards known as IFRS.

Despite the wish to be an independent body, the creation and direction of the IASB was heavily influenced by outside forces at this time. One of these forces was the European Union. At the time, the EU had no common set of accounting standards across its member nations. This generally created many smaller and fragmented capital markets spread throughout the EU. As a result, many looked to the United States, a much larger capital market, for investment. In order to address this problem, the European Commission sought to introduce a common set of accounting standards to the EU.

Naturally the EU would want to have some sort of control or influence over the creation of the accounting standards it adopted. Therefore, in 2000 during the development of the IASB, the European Commission made it clear that it intended to use IAS in the near future. This statement put an enormous amount of pressure on the IASC to become an independent body capable of producing high quality accounting standards. In 2002, the European Parliament and Council made the move to existing IAS and future IFRS official by forcing the use of said standards in 2005. This prompted the revision of many previous IAS to be at an acceptable quality for use in the EU. The adoption also highlighted the ability of the EU to influence the direction of standard making by the IASB.

Shortly before adoption, members of the EU were unhappy with IAS 32 and 39. The opposition to IAS 32 and 39 centered on the use of fair value for financial instruments and hedge accounting. Many nations in the EU, lead by France, looked to pressure the IASB into getting rid of the standards. The pressure came when the Accounting Regulatory Committee (ARC) recommended endorsement of all IAS except 32 and 39. IAS 32 was quickly revised and accepted, however, IAS 39 met more resistance. Following a revision of IAS 39, members of the EU were still unhappy. In response to this displeasure, the EC "carved-out" the pieces of IAS 39 that were the cause of most of the opposition (Brackney and Witmer 2005).

Outside influence at the time was not limited to only the adoption process for IFRS, but also the composition of the IASB. In 2005, 10 of the 19 trustees and 10 out of the 14 board members were from either the EU or the United States (Brackney and Witmer 2005). This convincing majority reflects the overwhelming "western" cultural influence present in the creation of IFRS. In addition to the large influence the EU has over IFRS, its system for endorsement does little to promote a truly uniform set of international accounting standards.

The European Union does not simply accept all new IFRSs that the IASB issues. Each addition to IFRS must make it through an endorsement process before it is put into practice in the EU. The process begins with the IASB issuing a new standard. After the standard is issued, the European Financial Reporting Advisory Group (EFRAG) begins to gather opinions from members of the private sector, including accounting professionals and other interest groups. The EFRAG will then use this information to advise the European Commission on endorsement of the standard. The advice offered is then evaluated for objectiveness and completeness by the Standards Advice Review Group (SARG). If the SARG gives its approval, the European Commission will then prepare a draft proposal. The Accounting Regulatory Committee (ARC) will then vote on the proposal. Once the proposal has passed, the European Parliament and Council of the European Union have three months to oppose the draft. The approval of the Parliament and Council or the passage of three months time results in the endorsement of the standard issued by the IASB. The entire process takes an average of seven months for completion (European Commission 2011).

The process of endorsement in by the EC can best be described as a screening process. The necessity of endorsement allows the EC to pick and choose which standards are best for them to use. This increases the potential for lobbying from members of the EU to try and avoid endorsing standards that do not fit their culture. This manipulation of the “single” set of standards is not limited to the EU. The effect of culture on international accounting can be seen throughout the present condition of IFRS.

Currently, IFRS has been adopted or is permitted in about 120 different jurisdictions. A list of nations and their status with respect to IFRS can be found in **Figure 1**. The IFRS foundation is composed of 22 trustees that are responsible for funding, oversight, and appointing the independent board members of the IASB, the Advisory Council, and the Interpretations Committee. The IASB is an independent 15-member board of preeminent accounting professionals from around the world. These members approve new IFRSs, exposure drafts, and interpretations. Funding for the board is generated by all jurisdictions that use IFRS currently or will in the future, and contributions are based on national GDP. The composition of the board is intended to be geographically diverse; however, expertise is the most important qualification for choosing board members. In an attempt to cement this intended diversity and to better represent worldwide interests, the board will be expanded to 16 members by 2012. The members will be divided as follows: four members from Asia/Oceanic; four from Europe; four from North America; one from Africa; one from South America; and two from any region.

The IFRS created by the IASB are a principle-based set of accounting standards. This allows for more flexible application of the standards and an increased use of professional judgment. It is also worth noting that there is no single body to enforce IFRS. Instead, each jurisdiction that uses IFRS enforces adherence to the standards which can be seen as a significant hindrance to the goals of the IASB.

According to the IFRS Constitution, the IASB's goals are: (1) to work to create a single set of accounting standards that are high quality, comparable, and relevant; (2) promote the use of those standards; and (3) bring about the convergence of international standards while maintaining high quality (IAS Plus 2011). One way in which the IASB aims to achieve these goals is through joint meetings with other accounting bodies such as the Financial Accounting

Standards Board (FASB) in the United States and the Accounting Standards Board of Japan (ASBJ). While these meetings are designed to work towards harmonization of global accounting standards, they also present an opportunity for jurisdictions to push their own agenda onto the IASB.

The FASB first announced its commitment to convergence with the IASB through the Norwalk Agreement in 2002. Since then, joint-meetings have been occurring between the FASB and IASB. Similar meetings have also been taking place between the IASB and the ASBJ. During these meetings, projects are proposed to bring about high quality solutions to differences in accounting standards. The relationship between the outside accounting bodies and the IASB allows for pressure to be applied in an attempt to make standards more compatible with one's own jurisdiction.

Both the history and the current state of IFRS have clearly been heavily affected by both the United States and the EU. Whether it be through funding, the adoption of IFRS in the EU, or the current convergence with US GAAP, the influence of these nations have significant implications for the compatibility of IFRS for jurisdictions around the world. As it pertains to culture, this influence implies a stronger pull towards the values of "western" societies.

According to Hofstede, these cultural values of "western" societies can be expressed through his cultural dimensions. For example, the United States and UK score highest in the dimension of individuality. The influence of strong individuality on IFRS can be seen through the creation of the IASB as an independent board comprised of professional accountants.

This classification of IFRS immediately presents a problem for the implementation of a single set of high-quality and internationally comparable standards. The cultural values that

IFRS can be associated with are not present everywhere around the world. Therefore, IFRS will meet resistance in these jurisdictions with dissimilar cultural values.

The author holds that the jurisdictions that do not quite align with IFRS express that difference in two ways. The first is through increased pressure on the IASB to change standards. This occurs through joint meetings and convergence between IFRS and other accounting systems. The second way is through carve-outs. Carve-outs illustrate that the adopting jurisdiction's accounting subculture does not match up with that of IFRS. The areas in which the carve-outs are placed can be used to see where values between the adopting jurisdiction and IFRS do not match.

In addition to the marginal differences in accounting values, there also exist cultural differences so vast between regions of the world that IFRS is cannot be truly comparable across all jurisdictions. For instance, cultural values in North America can differ greatly from those in nations in South America, and both differ from those values present in the Middle East. Both types of differences, marginal and vast, will be examined in the following chapters.

IV. Carve-outs

A jurisdiction adopting IFRS can be seen as a one with similar values that has aligned its accounting standards with those that exist under IFRS. However, this is certainly not always the case. There are still pervasive differences that exist between the two. Such differences are what trigger the use of carve-outs when adopting IFRS.

Carve-outs are an addition or omission of part of an accounting standard. These allow for modifications in the implementation of standards so that they may better fit the adopting societies' values. This type of adoption threatens the goal of international comparability held by the IASB. Unfortunately for the IASB, several jurisdictions have adopted the belief that the differences in values that exist between themselves and IFRS are too significant to be put into practice as they were written. The most notable of these was the carve-out of IAS 39 in the European Union.

European Union and IAS 39:

The resistance to endorsement of IAS 39 by the European Commission was voiced strongly in 2004, one year before the planned adoption of IFRS. The opposition was composed of several nations within the EU as well as the European Central Bank (ECB). The controversial aspects of IAS 39 revolved around the fair value option and hedge accounting (European Commission 2011).

The first issue, known as the fair value option, involved permitting the use of fair value to measure financial assets and corresponding liabilities. This part of the standard was originally put into place to allow for better matching. In other words, when a financial asset changed in value, its corresponding financial liability could also change in that period. However, the ECB objected to this fair value option, because it thought that banks might use the option to fraudulently write down financial liabilities in an attempt to meet capital requirements (Brackney and Witmer 2005). In response to the discontent related to the fair value option, the ARC issued a carved-out copy of IAS 39 which omitted the section allowing for the use of fair value for financial liabilities (ARC 2004). The ECB wanted this potential tool for escaping its regulatory requirements to be closed before the endorsement of IAS 39.

The IASB sought to meet this request by issuing a revision of IAS 39. An exposure draft was issued in an attempt to gain greater feedback on the problem. Based on feedback, the revision altered the fair value option by restricting its use. The carve-out was eliminated after the European Commission Regulations endorsed the change in the use of the fair value option to:

> situations where this results in more relevant information, because it either eliminates or reduces significantly a measurement or recognition inconsistency ('accounting mismatch')…Consequently, the application of the revised Fair Value Option is restricted to cases where certain principles or circumstances must be respected (European Commission 2005).

The removal of this carve-out was a step towards alignment of standards; however, it was not the only dispute with IAS 39 that existed. The second and more problematic carve-out was that of elements of hedge accounting.

Hedge accounting can be done in two ways: either through fair value hedge or a cash flow hedge. Fair value hedges occur when an entity attempts to offset the risk of a change in the fair value of an asset or liability. This is commonly done through either interest rate swaps or put options, which both help to lock in the current value of the instrument and protect against future change. The accounting for this type of hedge requires that both the original and hedging instrument be recorded at fair value on the balance sheet. The effect of this is a representation of the net risk that the entity is exposed to as a result of holding the hedged instrument. Finally, changes in the derivative used to hedge are shown through net income.

Cash flow hedges are defined as an attempt to mitigate the risk of changes in cash flows. Many times this is done through a futures contract. A futures contract locks in a price and quantity to be purchased at a future date. This allows for the offsetting of any increase in price in the desired good. Unlike fair value hedges, the changes in the derivative used in a cash flow hedge are shown as a change to the value of the hedged item (Kieso et al 2010).

The controversy over hedge accounting was created when banks voiced their discontent over the required use of cash flow hedge accounting for certain portfolio hedges. The EC stated in a Commission Regulation that it was not confident as to "whether IAS 39 sufficiently takes into account the way in which many European banks operate their asset/liability management, particularly in a fixed interest rate environment" (European Commission 2004). The banks argued that use of cash flow accounting was not effective and that portfolio hedges should have qualified as fair value hedges. As a result of the disagreement, the section of IAS 39 preventing fair value hedging of portfolio hedges was stricken from the standards endorsed by the EC.

The carve-outs of IAS 39 speak volumes about the difficulty in making IFRS a single-set of comparable standards. As referenced earlier, the EU had a considerable amount of influence over the direction of IFRS in the years immediately preceding adoption. Therefore, the fact that the largest market to adopt IFRS could not fully endorse the standards demonstrates that differences in values exist even in what appear to be very compatible circumstances. In addition, the EU set the precedent for creating region-specific versions of IFRS when the adopting party feels their circumstances have not been fully considered by the IASB, a practice that is ongoing currently in several areas considering adoption of IFRS.

Indian Accounting Standards:

A more recent example of deviations from IFRS can be seen in the case of India's convergence process. India first considered convergence with IFRS in 2006, when the Institute of Chartered Accountants of India (ICAI) proposed the change. The ICAI is the accounting standard creator for India. The proposition was followed by a concept paper in 2007 which outlined the convergence with IFRS and a planned adoption date of April 1, 2011.

Recently the ICAI has posted near-final exposure drafts of the new Indian Accounting Standards (Ind AS). The Ind AS are planned to be the new converged standards that will bring India closer to IFRS adoption. The posting of these standards was quickly followed by amendments issued by the Indian Ministry of Corporate Affairs (MCA). These standards and their amendments do not conform completely to IFRS. A Deloitte review of the differences, as of March 2011, listed 12 differences still in existence between the two sets of standards (Tracking IFRS 2011). However, the Chairman of National Advisory Committee on Accounting Standards in India stated that there are, "certain standards which to us do not make sense in the Indian context". These standards amount to four significant carve-outs including: business combinations; gain or loss on translation of foreign currency; fair value of liabilities; and construction contracts (Malegam 2011).

The difference involved in business combinations involves IFRS 3 and Ind AS 103. The two standards disagree upon the treatment of a bargain purchase. A bargain purchase occurs when one entity purchases another for less than its fair value. An acquisition of this nature is thought to result in a gain for the acquiring entity, because it is paying less for the whole than the sum of the parts. Under IFRS 3 the gain on a bargain purchase is shown in the profit or loss account (Tracking IFRS 2011). Ind AS 103 differs, firstly, by requiring that there be significant evidence to show that the acquisition being made is really a bargain purchase. The second difference is that the gain from said purchase will be shown through other comprehensive income. This change is based on the belief that the acquisition is not part of the entity's normal business operations, and therefore should not be shown through profit or loss (Malegam 2011)

A gain or loss on translation of foreign currency is covered by IFRS 1 and Ind AS 101. Issues can arise in the translation of foreign currency when an entity borrows foreign capital in a foreign currency over a long period of time. IFRS dictate that the entity must calculate the outstanding balance at the end of each year at the current exchange rate. Then any difference that exists through the translation is taken as a gain or loss in the current period. Indian standards do not comport with this approach. Instead entities reporting under Indian standards have the option of recognizing the difference in equity and amortizing it over the life of the loan (Tracking IFRS 2011).

The justification for this change lies in the nature of Indian business. If an Indian entity requires foreign funding, the entity must issue a bond in foreign currency. Malegam argues that this is ignored by many of the larger supporters of IFRS such as the US, the UK, and EU, because they can issue bonds to foreign entities in their own currency. As a result of the frequency with which Indian firms must do this, there is a desire to smooth the borrowing costs over the term of the bond.

The third carve-out stems from the ability to make adjustments to the fair value of financial liabilities. This concept is the same as that which is present in IAS 39, discussed earlier in this chapter. The recently amended Indian standards allow for adjustments to these financial liabilities due to changes in the market interest rate. However, they do not permit the adjustments allowed to be made due to the change of an entities rating which are allowed under IFRS (Tracking IFRS 2011). This simply means that under the Indian system the change in interest rate related to the increased or decreased risk associated with the entity is not grounds for an adjustment in value of financial liabilities.

The final carve-out present in Ind AS can be found in the revenue recognition in construction contracts. Like many current accounting standards IAS 11 calls for the percentage of completion method to be used for construction contracts. The percentage of completion method allows for the recognition of revenue to be spread out over the length of a long-term contract based on completion. This is done by assessing the completed costs of a project as a percentage of the total costs. Then this percentage of costs incurred is multiplied by the expected revenue from the project to calculate the portion of revenue that can be recognized.

Ind AS 11 and IAS 11 both permit the use of the percentage of completion method for revenue recognition. However, IFRS, through IFRIC 15 *Agreements for Construction in Real Estate*, imposes an exception to the use of this method. IFRIC 15 specifies that if the buyer does not have the ability to control structure design before and during the construction process, then the deal my not fall under the scope of a construction contract. This could be the case if the build also requires a service to be performed before the contractual obligation is met. When these criteria are fulfilled, the contract will be treated as a sale of goods, and therefore, revenue will not be recognized until all obligations are satisfied (IAS Plus 2011). The final carve-out in the Ind AS is the omission of IFRIC 15.

India is a nation that can certainly be said to have had significant "Western" influences in its development. However, those influences are still not nearly enough for all of Indian accounting values to align perfectly with IFRS. As Malegam simply stated, there are "certain standards which to us do not make sense in the Indian context". The differences that still exist between the values embodied by IFRS and those present in the Indian system are not trivial. This becomes all the more evident after examining statements made in the ICAI's concept draft, which stated, "only in rare instances of public interest will a carve out from an IFRS be made" (ICAI 2007). The ICAI referred to an incompatible economic environment and a lack of industry preparedness. It then follows that the four carve-outs that have been discussed previously are a result of societal differences.

The types of societal differences can be partially uncovered by examining the carve-outs themselves. For instance, all four carve-outs listed in some way or another attempt to eliminate volatility by smoothing earnings, losses, or expenses over a longer period of time. This tendency to avoid volatility can be expressed through Hofstede's cultural dimensions as a higher level of uncertainty avoidance.

As more regions look to adopt IFRS, the practice of carve-outs will continue, and therefore, increase the number of jurisdiction-specific versions in existence. The more each jurisdiction tailors IFRS to its own culture the less likely the goal of international accounting harmonization becomes. However, the pervasiveness of carve-outs is not the only problem that culture creates for international comparability. There are such a vast variety of cultural identities in the world that implementation of any single set of standards is not possible.

V. Culture and Accounting

The largest hurdle facing the implementation of a single set of high-quality international accounting standards is the vast array of societal values embodied in different cultures. These values are inherently interconnected with many defining aspects of society such as: language, religion, education, and economy. Therefore, differences in values are accompanied by differences in crucial aspects of society, and it is these numerous differences that can make it incredibly difficult to apply one set of standards to the entire world.

The diversity that exists in cultural values can be seen through the cultural dimension scores measured by Hofstede. Scores for both IFRS and local GAAP-using jurisdictions can be seen in **Figure 2**. This figure displays the varying values that occur between different countries, including ones that have adopted IFRS. The four dimension scores for the listed nations illustrate the variety of values both within and between regions.

There is a significant distance in values in North America between the United States and Canada and Guatemala and Mexico. The largest differences appear in the scores of power distance, individualism, and uncertainty avoidance. The US and Canada both have scores that convey relatively low power distance and uncertainty avoidance and high individualism, whereas Guatemala and Mexico have scores that display the exact opposite. These values demonstrate the differences that can exist between countries that share borders.

An even more telling set of values are those of the three nations in Europe. Not only do all of these nations belong to the European Union, they all consequently have adopted IFRS. Even though they share these commonalities, they still differ in power distance, individualism, and uncertainty avoidance. What makes this even more interesting is that the two values that Gray postulates have the highest correlation to accounting values (individualism and uncertainty avoidance) show the most significant variance between the three countries. France posses the highest score for uncertainty avoidance of the three nations, and was a major proponent of the carve-outs to IAS 39. This truly exposes the conflicting values that are present between countries that share the same accounting system.

Finally, there are differences present in the data that illustrate just how unalike two cultures can really be. Take for example, the dimension scores for the UK and Pakistan. The UK scores 35, 89, 66, and 35 on power distance, individualism, masculinity, and uncertainty avoidance. Conversely, Pakistan has scores of 55, 14, 50, and 70, respectively, making the two nations polar opposites in terms of cultural value scores. The discrepancies seen between countries make apparent the difficulties the IASB faces when trying to create a set of standards that will be comparable worldwide.

There are several factors that can cause one country to be so different from another culturally. The first area that presents an obstacle for implementation is language. It is an accepted concept that language carries with it values and meaning. Each language imparts those values and meaning into laws and rules, such as accounting standards. Language also presents a problem because its meaning can be destroyed or construed through translation. This pertains to IFRS, because in order for it to be used internationally it must be translated into many languages. The IASB, therefore, must go to great lengths to ensure that standards retain the meaning with which they were originally written.

The process for translation of IFRS involves the identification of key terms. Those key terms then have to be approved by the Committee. Once they are approved they are used to translate IFRSs with the help of computer software. Finally, the text is reviewed by the Committee, and if approved, finalized (IFRS Foundation 2011). While this process if thorough, it is not perfect. It is inevitable that IFRS will lose some of their meaning in translation.

Religion is also another factor that has a strong influence over the behavior of individuals and societies as a whole. It is plausible that religion influences every one of Hofstede's dimension. As a result religion has the potential to be a strong driving force in the method through which economic transactions are handled and how they are accounted for. One such religion is Islam.

Islam, which can be translated to mean "submission or surrender, understood to be the will of God" (Ali and Leaman 2008), is the second largest religion in the world. It is prevalent throughout Africa and Asia, and more specifically the Middle East. Those that follow Islam, Muslims, do so through their holy texts. The first is the *Qur'an* which is believed to be the will of God as told through the Prophet Muhammad. The second is the acts and sayings of Muhammad known as the *Sunnah*. The two form what is known as the *Shari'ah* or "the path". Muslims look to follow this path through all aspects of life, including business (Hamid et al. 1993).

Muslims, therefore, follow the ethical principles and rules as dictated by Islam throughout their economic dealings. Under Islam, all property is considered to be God's property and Muslims are only holders. Therefore, this property must be "used for the common good, not exploited" (Hamid et al. 1993). Consequently, the charging of interest is strictly forbidden, because it is deemed to unfairly guarantee a gain to one party without assuming the risk of loss. Instead gains on loans made are contingent on a determined rate on the gains experienced by the borrower.

In addition, one of the five pillars of Islam, *zakat*, requires a redistribution of excess wealth from the "privileged" to the "underprivileged". *Zakat* requires the valuation of assets in a religious context, therefore, rendering any sort of historical cost accounting ineffective (Hamid et al. 2008). Clearly this creates a distinct difference from western accounting.

To address the specific accounting needs of Islamic organizations, the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) has developed standards that consider the following of *Shari'ah*. The standards set by the AAOIFI have been implemented in six countries, and guidelines have been based upon theirs in five others (AAOIFI 2011). The existence of these separate standards presents a unique problem to the implementation of IFRS, because of the stark differences related to the absence of interest and inclusion of *zakat*. As no part of IFRS offers guidance for following *Shari'ah*, it seems likely that any Islamic nation adopting IFRS would do so while allowing for the large exception of accounting for financial institutions using AAOIFI standards.

Another factor that represents differences in societal values is education. The value placed on the level and type of education in a society would most likely be reflected through a change in the dimension of masculinity, with increases in educations geared toward monetary gains and success increasing the masculinity score. The level and direction of education also can affect a nation's ability to develop and implement accounting standards. In many instances a country's educational system does not place a high value on the study of accountancy. This results in a lack of qualified and educated accountants to develop and implement high quality standards. A prime example of this kind of situation is Africa.

Africa presents a wide variety of accounting education and experience. The progression of accounting ranges from the experienced IFRS implementers in South Africa to the French influenced nations of Northern Africa. As a result, there still exist many locations in Africa where there are too few qualified accountants to effectively implement a complex set of standards such as IFRS. A manager for the African Development Bank, Jerry Mutonga echoes this sentiment: "the number of qualified accountants in Francophone countries is so limited. It will take years to get to the technical capabilities required. Even with a simplified version of IFRSs they will not be able to comply in the next 10 years. By 2020 they would struggle to comply" (Bruce 2011). Several nations in Africa do not have the necessary resources, training, and educational institutions to produce a large enough group of accountants to expedite the implementation of IFRS. Similar situations can be found any place that there is an absence in higher education or in the value of education in general. The scarcity1 of educated accountants in certain areas will greatly slow down the process of adoption of IFRS around the world.

In addition to language, religion, and education, the state and characteristics of a country's economy can have an effect on a nation's cultural values. Certainly the style of one's economy will be reflected through at least two of Hofstede's cultural dimensions. For example, a highly developed capitalist economy should promote a higher value in individualism and power distance as well as a possible increase in masculinity. This type of an economy will also affect the type of accounting system in place. A western economy will promote western accounting standards and a better alignment with IFRS, whereas economies driven by socialist tendencies or perhaps even religious values will produce different accounting systems that require more work to be receptive to IFRS.

Hofstede's scores of nation's cultural dimensions as well as a discussion of culture and its aspects of society that are interrelated, paints a clear picture of the sheer number of societal values present in the world. The multitude of values consequently presents a serious road block to the realization of the IASB's goal of international comparability, because it becomes so difficult to implement a truly uniform set of standards upon so many potentially conflicting values.

VI. Conclusion

The goal of convergence as well as the eventual comparability of international accounting standards is a feat that cannot be achieved without the consideration of the cultures of the adopting jurisdictions. Previous works have established that there is a connection between a society's culture and the accounting system that it uses. Therefore, the differences that exist between the values of nations will translate to differences in accounting systems. The IASB has the daunting task of addressing all of these differences to try and bring about international convergence.

This goal has been met with resistance, however. Many adopting nations have done so only through locally endorsed IFRSs. This has allowed for nations to make carve-outs to IFRS to better mold it to their own values. As a result, there is not one set of standards, but several sets that are each specific to the jurisdiction making the changes. The IASB also faces the challenge of applying IFRS to societies that don't align well with the western influences present within the standards. These societies have such stark differences in aspects such as language, religion, education, or economy that at the present moment do not align well with IFRS. The most obvious being Islam and the very specific method of accounting that entities abiding by its rules must follow.

The combination of all these forces acting against the implementation of a uniform, comparable set of accounting standards leads the author to postulate that true worldwide comparability cannot be achieved in the foreseeable future. For this reason standard setters should work to better understand the cultures in the regions that are so underrepresented (Africa and the Middle East) in the standard formation process. Doing so will diversify the input given in the creation of IFRS, and hopefully result in a better representation of societal values, thus smoothing out the convergence process.

Appendix

Figure 1: IFRS by Nation

	IFRS Required	IFRS Permitted	Possible Future Adoption	Version
North America				
Antigua and Barbuda	Y			IASB
Aruba	Y			IASB
Bahamas	Y			IASB
Barbados	Y			IASB
Bermuda	N	Y		IASB
Canada	Y			IASB
Cayman Islands	N	Y		IASB
Costa Rica	Y			IASB
Dominican Republic	N	Y	2014	IASB
El Salvador	N	Y		IASB and Local
Guatemala	N	Y		IASB
Honduras	Y			IASB
Jamaica	Y			IASB
Mexico	N	Y	2012	IASB
Netherland Antilles	Y			IASB
Nicaragua	N	Y		IASB
Panama	Y			IASB Modified for Banks
St. Lucia	Y			IASB
Trinidad and Tobago	Y			IASB
United States	N	Only foreign private issuers	2015	LOCAL GAAP
South America				
Argentina	N	N	2012	LOCAL GAAP
Bolivia	Y			IASB
Brazil	Y			LOCAL IFRS
Chile	Y			IASB Modified for Banks
Colombia	N	N	2012	
Ecuador	Y			IASB Translated to Spanish
Paraguay	N	N	2014	
Peru	Y			LOCAL IFRS
Uruguay	Y			LOCAL IFRS
Venezuela	N	Y	2011	IASB *IAS29
Europe				
Albania	Y			IASB

Austria	Y			EU IFRS
Belgium	Y			EU IFRS
Bulgaria	Y			EU IFRS
Cyprus	Y			EU IFRS
Czech Republic	Y			EU IFRS
Denmark	Y			EU IFRS
Estonia	Y			EU IFRS
Finland	Y			EU IFRS
France	Y			EU IFRS
Georgia	Y			LOCAL IFRS
Germany	Y			EU IFRS
Greece	Y			EU IFRS
Greenland	Y			EU IFRS
Hungary	Y			EU IFRS
Iceland	Y			EU IFRS
Ireland	Y			EU IFRS
Isle of Man	N	Y		IASB OR EU IFRS
Italy	Y			EU IFRS
Lithuania	Y			EU IFRS
Luxembourg	Y			EU IFRS
Macedonia	Y			LOCAL IFRS
Malta	Y			EU IFRS
Moldova		N	2012	LOCAL IFRS
Montenegro	Y			IASB
Netherlands	Y			EU IFRS
Norway	Y			EU IFRS
Poland	Y			EU IFRS
Portugal	Y			EU IFRS
Romania	Y			EU IFRS
Russian Federation	Y			IASB
Serbia	Y			LOCAL IFRS
Slovak Republic	Y			EU IFRS
Slovenia	Y			EU IFRS
Spain	Y			EU IFRS
Sweden	Y			EU IFRS
Switzerland	N	Y		IASB
Ukraine	(for public joint stock companies)		2012	IASB
United Kingdom	Y			EU IFRS
Asia				

Afghanistan	N	Y		IASB
Armenia	Y			IASB
Azerbaijan	Y			LOCAL IASB
China	N	N		LOCAL GAAP
Hong Kong	N	Y		IASB
India	N	N	2011	INDIAN IFRS
Indonesia	N	N		LOCAL GAAP
Israel	Y			IASB
Japan	N	Y	2012	LOCAL IFRS
Kazakhstan	Y			IASB
Korea (Republic of Korea)	Y			IASBTranslated
Kyrgyz Republic	Y			IASB
Lebanon	Y			IASB
Macao Special Administration	Y			LOCAL IFRS
Malaysia	N	foreign	2012	LOCAL GAAP
Pakistan	Y			LOCAL IFRS
Philippines	Y			LOCAL IFRS
Qatar	Y			IASB
Saudi Arabia	(for banks)			IASB
Singapore	N	Y	2012	LOCAL IFRS
Taiwan	N	foreign subsidiaries or on local exchange		
Thailand	N	N	2013	LOCAL GAAP
Turkey	Y			EU IFRS
Uzbekistan	Y			IASB
Vietnam	(for banks)			IASB
West Bank/Gaza	N	Y		IASB
Africa				
Angola	N	N		LOCAL GAAP
Botswana	Y			IASB
Cameroon	N	N		LOCAL GAAP
Cote D'Ivoire	N	N		LOCAL GAAP
Democratic Republic of Congo	N	N		LOCAL GAAP
Egypt	N	N		LOCAL GAAP
Equatorial Guinea	N	N		LOCAL GAAP
Gabon	N	N		LOCAL GAAP
Ghana	Y			IASB
Kenya	Y			IASB
Madagascar	N	N		LOCAL GAAP

Malawi	Y			IASB
Mauritius	Y			IASB
Morocco	(banks and financial institutions)	Y		IASB OR EU IFRS
Mozambique	Y			LOCAL IFRS
Namibia	Y			IASB
Nigeria	N	N		LOCAL GAAP
Republic Congo	N	N		LOCAL GAAP
Senegal	N	N		LOCAL GAAP
South Africa	Y			IASB
Swaziland	Y			IASB
Tanzania	Y			IASB
Uganda	Y			IASB
Zambia	Y			IASB
Zimbabwe	Y			LOCAL IFRS
Oceana				
Australia	Y			LOCAL IFRS
New Zealand	Y			LOCAL IFRS

IASB denotes IFRS as issued by the IASB
LOCAL IFRS denotes IFRS as adopted locally
EU denotes IFRS as adopted by the European Union
() exception to a not required status

Source: PwC. IFRS Adoption by Country. 2010

Figure 2: Hofstede's Cultural Dimensions

	Power Distance	Individualism	Masculinity	Uncertainty Avoidance	IFRS Permitted
North America					
Canada	39	80	52	48	Y
Guatemala	95	6	37	101	Y
Mexico	81	30	69	82	Y
United States	40	91	62	46	N
South America					
Argentina	49	46	56	86	N
Brazil	69	38	49	76	Y
Chile	63	23	28	86	Y
Europe					
France	68	71	43	86	Y
Germany	35	67	66	65	Y
UK	35	89	66	35	Y
Asia					
Japan	54	46	95	92	Y
India	77	48	56	40	N
Indonesia	78	14	46	48	N
Pakistan	55	14	50	70	
Africa					
West Africa*	77	20	46	54	N/A
South Africa	49	65	63	49	Y

*Ghana, Nigeria, Sierra Leone

Source: Itim International. 2011.

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