*International Journal of Business and Management Invention (IJBMI)*
*ISSN (Online): 2319 – 8028, ISSN (Print): 2319 – 801X*
*www.ijbmi.org || Volume 7 Issue 5 Ver. II || May. 2018 || PP—21-26*

# The Classification of the Accounting Systems

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***ABSTRACT:*** *The financial reporting activities of the enterprises in a country for a specific period constitute the accounting system of that country. In this context, accounting systems can be classified on the basis of a large range of factors, varying from the method adopted in recording financial events to how these events are audited, to the qualifications of the accounting professionals and to the accounting rules followed. The objective of this paper is to present the most important classifications of the accounting systems and to show what could be done in the near future*
***KEYWORDS:*** *International Accounting, Accounting Systems, Classification*

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Date of Submission: 20-04-2018 Date of acceptance: 05-05-2018

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## I INTRODUCTION

It is a common secret that globally we don't have the identical accounting practices among the countries. However, many countries are facing the same influences. The last years the European Union is promoting the process of accounting unification and all the recent studies and researches are subject to major changes. Although the changes of the accounting systems still have many differences. Thus, relevant for the international context are the legal, cultural, historical differences even between the EU member states (Sforza, V. and Cimini, R., 2017). The awareness of this diversity and the demands which are imposed by the globalization, have led nowadays to the phenomenon of the harmonisation of the accounting standards by IASB and the European Community.

The most valuable tool for comparing the different national accounting regulations and practices in order to group countries is the classification of the accounting systems. The classification will provide elements that characterize a country's accounting system, without the need to know all their rules and accounting practices. It is very important to mention that the accounting classifications have as starting point the similarities between the accounting rules and practices within countries, and from the other side the accounting harmonisation is based on the differences existing between rules, accounting practices, in the same country or from different ones. Despite the fact that we have different starting points the essential role of the accounting classification is to assess the difficulties of carrying out the international accounting harmonisation policies.

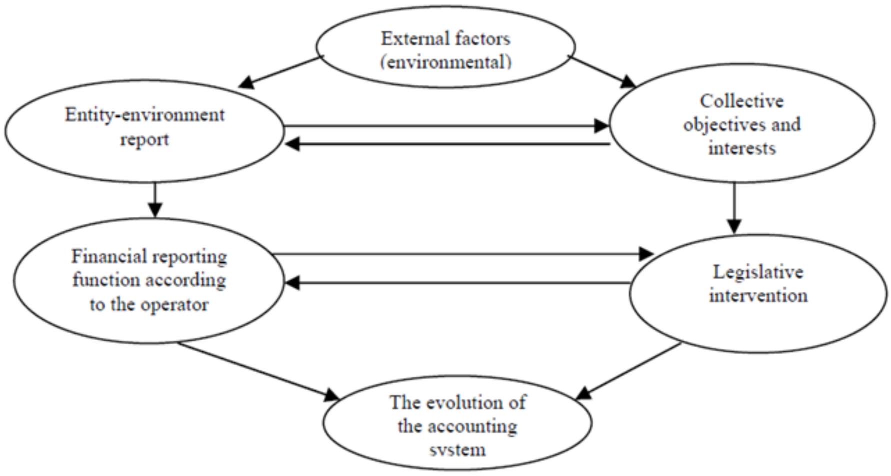
In this paper we are using qualitative research which is based mainly on interpretation. We have collect the most important papers and researches in the field of the International Financial Reporting Standards (IFRS) and we are trying to find and understand the differences and similarities between the national accounting systems which are absolutely necessary for international accounting harmonisation. According to Nobes (2011), classification "is a fundamental process in the better understanding of phenomena", so we will try to present the main approaches which are accepted by the literature of the field. In addition we consider that the classification made by Nobes in 2011 expresses on the best way the fact that the international accounting harmonisation specialists are still facing problems arising from the national practices.

## II INTERNATIONAL ACCOUNTING

According to the literacy international accounting is defined as the science which studies the reasons for the differences between accounting systems as well as the functions associated with the international financial reporting system. According to an ancient Greek philosopher, Aristotle, has written: "if you would understand anything, understand its beginnings and development." So therefore, it will be appropriate to have historical look back about the emergence of the international accounting. The importance of international accounting can be attributed to its past developments. Accounting as we find it nowadays is the result of many combined efforts of number of different nations. The Double entry system was originated in Italy and from Italy it was spread to many other European countries. In the 18th century English people became instrumental to play an important role in transferring accounting and auditing not only to the USA but also to other countries. In the beginning of 20th century USA emerged as a super power not only in the field of political developments but also in the developments of accounting theory and practices. USA is dominating and in the development of accounting literature. Institutes like AAA and AICPA are playing an essential role in spreading the US accounting methods thought and practices to the European countries. So, it can be concluded that accounting has always been international from the time of its origin in Italy. According to Parker (1983) "Modern accounting is not the invention of one country; it has always been international in its scope". There are four different approaches to the definition of International Accounting:

1. World Accounting: According to this approach the International Accounting is a universal system of accounting which is easily acceptable in all the countries.
2. Comparative International Accounting: Under this approach International Accounting includes all varieties of accounting principles and methods of accounting in all the countries throughout the world.
3. Operational International Accounting: This approach covers the particular technical problem being faced by domestic corporations and multinational corporations in foreign business. These are typical operational problems like foreign currency translation, consolidation, foreign exchange risk management etc.
4. Politicized International Accounting: This approach emerged from the involvement of global political institutions such as UNs which their main task is to bring harmonization in divergent IA practices.

**Figure 1: the influence of the external factors on IE**




Source: Aureli, S.,(2015)

## III THE IMPORTANCE OF INTERNATIONAL ACCOUNTING

A number of factors have led to increased emphasis on IA in new millennium. Some of them are listed below:

- Rapid developments in foreign trade: in the early stages of civilization foreign trade was existed, when the caravans used to travel from country to country. Means of transportation have led to change in volume and character of foreign trade. Mobility of labor - broke new records, creating new world markets for goods, services and capital. This changed face of foreign trade, has given rise to a number of unique accounting problems which further led to the need of specialized branch of accounting having an International dimensions
- Increased number of multinational companies: Multinational Company is a form of business organization which operates in more than one country. The number of such companies is increasing with the passage of time. This increased number of multinational companies on the international scene can be considered a single largest cause responsible for enhanced importance of IA. MNCs also play a dominating role in boosting accounting reforms. For instance any MNC operating in two countries like India and Iran has to prepare consolidated financial statements by incorporating accounts of both subsidiaries having different accounting environment by providing a uniform basis for preparation of financial statements.
- Global capital market: The capital market is the market where from productive capital is raised and made available for development purposes. The flow of capital has crossed national boundaries in recent years. Internationalization of capital market has led to the concept of global capital market. The concept of global capital market concentrates on providing reliable and comparable financial information to investors belonging to different countries. Uniform accounting principles and practices can help the participant companies in global market to provide comparable financial information to investors. IA will be helpful to eliminate barriers or obstacles in free flow of international capital.
- Environmental awareness: Environmental accounting has become part and parcel of IA. Efforts are being made to make corporations all over the world environment sensitive so as to adopt green accounting as a part of IA.

- Historical precedents: Historians are of the view that accounting has passed through different phases of developments after its emergence in the form of recording activity. Accounting as it seems today in its present form as a modern accounting system is an outcome of a historical process which initiated in ancient civilization and ended in highly developed industrial society. The successive stages of evolution of scientific accounting passed through various periods of pre-capitalistic, commercial capitalism, industrial capitalism and finally in the present periods. So we can conclude heritage of accounting is truly international in nature.
- Divergent accounting practices: Accounting practices differ from one nation to other may be probably because of primarily different national or regional patterns of accounting developments. Accounting being language of business should speak and convey same meaning to users of financial statements irrespective of the place to which they belong to, whether India, Japan or USA. IA attempts to develop this common language for users of financial statements.
- Emergence of e-business on global scenario – Concept of e-business which emerged in developed countries has entered in developing and in underdeveloped countries at a very rapid speed. This concept of e-business has posed number of international problems. IA may help accounting professionals not only in sorting out such problems but also solving them too.

## IV TYPES OF CLASSIFICATION SCHEMES

Bogdan (2014) noted that the first attempts in order to classify the accounting systems are dated about a century ago. It was 1911 when Hatfield's classification was formed and it was consisted of three groups: USA, the United Kingdom, Northern Ireland and the continental Europe). The researcher's interest was increased in the decade of 60s. In the decade of 70s emphasis was placed on the empirical grounding of the undertaken studies while in the 80s and 90s the most important part of international accounting research was constituted.

Nobes and Parker (2008) in an innovated research proposed a classification of the accounting systems using the taxonomy extrinsic (deductive) and intrinsic (inductive). The deductive approach implies that the classification of the accounting systems is based on the identification of the relevant environmental factors (legal system, tax system, culture, level of economic development, etc.). In the other hand, the inductive approach implies that the classification of accounting systems is based on the analysis of accounting practices.

According to the literacy 1967 was the starting point of the deductive analysis of the accounting systems. At that year Mueller identified four development models for accounting systems such as macroeconomic and microeconomic accounting as an independent discipline and uniform accounting (Gray, 1988).

## V THE AMERICAN ACCOUNTING ASSOCIATION MORPHOLOGY OF ACCOUNTING SYSTEMS

The second important attempt to classify the Accounting Systems was made in 1977 by AAA (American Accounting Association). It was an attempt to describe all the major characteristics which are influencing the accounting systems. Roberts et al, (2005) stated that the American Accounting Association identified eight influences called accounting system "parameters": political system, economic system, economic development, financial accounting objectives, the origins of accounting norms, education and accounting training, enforcement of ethical norms, the client (Roberts et al, 2005). Based on this morphology, the American Accounting Association identified five influence zones: British, French-Spanish-Portuguese, German- Dutch, communist and American. (Bogdan, 2004)

**Figure 2: AAA's proposed morphology of accounting systems**

| Parameter | States of nature | | | | |
|---|---|---|---|---|---|
| | 1 | 2 | 3 | 4 | 5 |
| $P_1$ Political system | Traditional oligarchy | Totalitarian oligarchy | Modernizing oligarchy | Tutelary democracy | Political democracy |
| $P_2$ Economic system | Traditional | Market | Planned market | Plan | – |
| $P_3$ Stage of economic development | Traditional society | Pre take-off | Take-off | Drive to maturity | Mass consumption |
| $P_4$ Objectives of financial reporting | Investment decisions | Management performance | Social measurement | Sector planning and control | National policy objectives |
| $P_5$ Sources of/ authority for standards | Executive decree | Legislative action | Government administrative unit | Public–private consortium | Private |
| $P_6$ Education, training and licensing | Public informal | Public formal | Private informal | Private formal | – |
| $P_7$ Enforcement of ethics and standards | Executive | Government administrative unit | Judicial | Private | – |
| $P_8$ Client | Government | Public | Public enterprises | Private enterprises | – |

Source: American Accounting Association (1977)

## VI NOBE'S STUDIES

During the last decade of the 20th century (between 1990 and 2000), other researchers have proposed new accounting system classifications. The most important was Nobes' theory which establishes the differentiation factors. These factors allow an accurate classification of the accounting systems about: the typology of users of accounting information from financial reports of listed entities, the degree in which laws and standards impose details while excluding subjective judgments, about the importance of taxation rules, the caution and precision in applying historical cost, about writing practices of consolidated financial reporting and about the entity uniformity in rule application.

The first hierarchical classification was set up in 1983 by Christopher Nobes and it was based on the financial reporting system (Novas et al, 2017). This system is identifying two orientations: micro and macro and were grouped into subclasses, families and species.

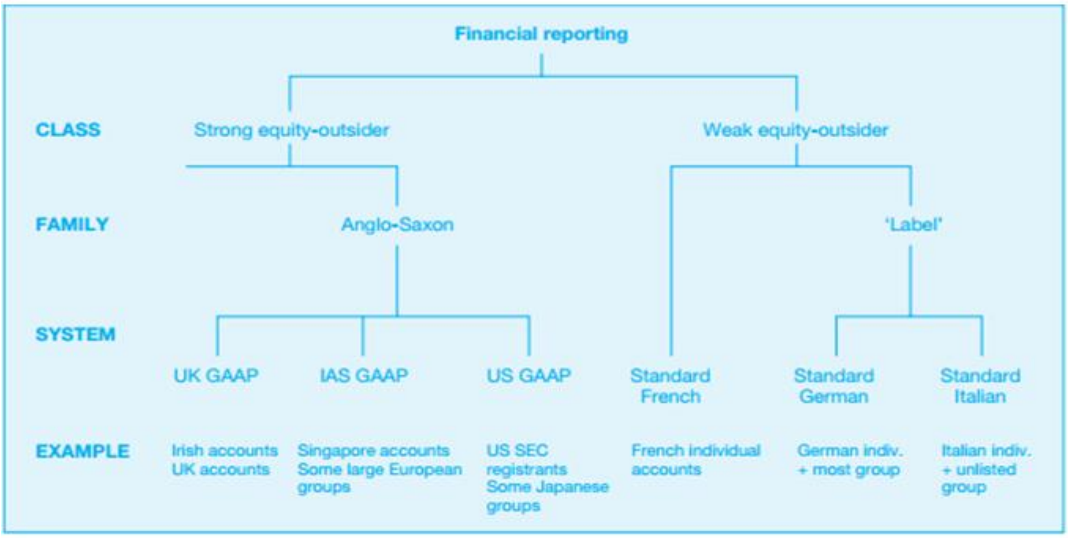
The microeconomic-oriented countries are prevailed by the elements of judgment; the concept of fair view and the market-based economic adjustment. According to this view we have Holland (which is strongly oriented towards business), Australia, New Zeeland, the United Kingdom and Ireland (with professional rules derived from business practices of British origin), Canada and the United States (with professional rules derived from business practices).

The macroeconomic-oriented countries are predominant by uniformity in the application of measurement methods (Tabara et al, 2010). Examples according this view are Italy (with a system based on the Civil Code and international influences), France, Belgium and Spain (with an accounting system based on unified account plans), Germany and Japan (with an accounting system based on statutory rules) and Sweden (with an accounting system based on economic control imposed by the tax system.

In his research in 1988, Gray realized that the importance of culture does not seem to be fully appreciated. Thus, based on Hofstede's study of 1980, identified four cultural values which are influencing the accounting practices (Gray, 1988). These four cultural values were professionalism, versus statutory control, uniformity versus flexibility, conservatism versus optimism and finally secrecy versus transparency. The Gray's model based on cultural influences was a way to show the impact of culture on accounting and the connection between culture, accounting values and accounting practices (Cigdem, Sonan, 2007).

According to Saita et al (2012), on an international level there is a need to distinguish countries between credit countries/insider (countries which are financed mainly by banks) and equity countries/outsider (countries financed directly by investors). This point is very important because these differences affect the international financial reporting standards. In his study Nobes (1988) pointed out that one of the most important factors to explain any difference among the accounting systems is the financing system which is varying from country to country. Hence, he divided the financial reporting systems into two classes. The strong equity – outsider, in which we can find countries with strong funding through external equity, corresponding to the Anglo-Saxon systems such as United Kingdom and New Zeeland. The second class is the weak equity – outsider. In this class we can find countries with low equity corresponding to the continental Europe accounting systems (Nobes and Parker, 2008).

**Figure 3: Nobes's proposed hierarchical classification of accounting systems (1998)**

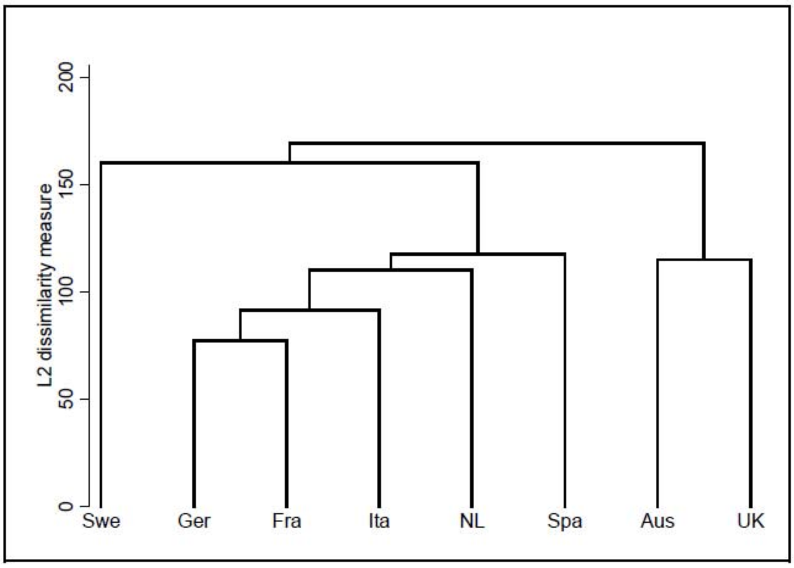



Source: Roberts, C., Weetman, P., Gordon, P, 2005

During 2008, Nobes started to wonder if the previous accounting classifications are still relevant in the "IFRS era". Therefore two years later in 2010, with Erlend Kvaal, performed a study in which they have examined the IFRS practices of five countries Australia, France, Germany, Spain and Great Britain.

They have collected and analyzed the financial statements for the financial years 2005 and 2006 for the major companies listed in these countries. The financial statements were from a number of 232 companies of various fields of activity). The authors stated the existence of national practices different from the IFRS ones. Then they analyzed the financial statements for the years 2008-2009, and they found the same occurrence. In 2011, Nobes research attempt to investigate whether the classification made in 1983 leading to the creation of two groups is still valid even after 30 years. Out of the 14 countries included in the classification, Nobes gathered data for eight of them. In this research his sample was from Australia, France, Germany, Spain, the United Kingdom, Italy, Sweden and Holland. For the 287 of the financial statements, 13 criteria were used. Six of them referring to the presentation practices and seven referring to measurement practices.

**Figure 4-Accounting system classification by Nobes.**




Source: Nobes, C., (2011)

Figure 4 represents the results. All statistical techniques have led to the same conclusion: the Anglo and continental European groups can be identified in the IFRS practices of large companies (Figure 4). The national accounting practices are being resistant to the harmonisation process. (Nobes, 2011). As we can see from Figure 4, Germany and France form the first pair of countries and together form a single unit. Germany and France together with Italy form another pair. They, in turn, form another unit which, coupled with Holland. Thus, another unit is formed which, together with Spain form the other pair. Australia and Great Britain form a pair in the Anglo group.

## VII CONCLUSION

As we have seen from the discussion above the classifications of accounting systems have been developed using a variety of different approaches and there often appeared to be little in common between many of the studies.

The deductive studies are classifying accounting systems on the basis of a wide range of different economic and cultural factors. The main contribution of the deductive studies is not so much to offer classifications of particular countries, but to offer descriptions of the key features of national accounting systems and to suggest which factors are influential in their development.

From the other hand we have the inductive studies which offer a quite different way of developing a classification system. The inductive studies have a number of weaknesses, particularly the misuse of statistical tests and unthinking use of large data sets. They have also used different types of data and included different countries and different time periods. It is not surprising that the results of the different classification studies are not always consistent.

There are several possible ways to follow in the near future. One solution could be the use of the increasingly sophisticated statistical methods alongside databases that have been specifically developed for the purpose of classification. With that way we could undoubtedly lead to better classifications as many of the problems of the existing classifications could be avoided. These new classifications will not probably be significantly better or different from those of the past. What could be done is to develop new and significantly improved or more useful data sets of accounting rules and practices and to decide which rules and practices are important and vary in a consistent and predictable manner across countries, and which occur randomly or are temporary or trivial. The most useful way in the future is therefore not to carry on replicating past studies using improved data sets or statistical tests, but instead to concentrate upon detailed individual country case studies.

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Stylianou Tasos." The Classification of the Accounting Systems" International Journal of Business and Management Invention (IJBMI) , vol. 07, no. 05, 2018, pp. 21–26.