

## **IFRS FOR SMES: CULTURAL DIMENSIONS ON ACCOUNTING IN CENTRAL AND EASTERN EUROPE COUNTRIES**

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### **Abstract**

*The aim of this paper is the impact evaluation of cultural dimensions on accounting in CEE countries concerning the adoption process of IFRS for SMEs. In achieving this aim, we identified the cultural characteristics of CEE countries using two basic models of cultural dimensions: the six dimensions of Hofstede (1980, 2010) and Gray's values (1988). The sample selected was analysed for Hofstede's dimensions and a similar accounting profile based on Gray's values. Further, we compared the profile of each jurisdiction to a favourable profile proposed by Borker (2012a) for the adoption of IFRS.*

**Keywords:** IFRS for SMEs, accounting values, cultural dimensions

**JEL classification:** M40, M41

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### **1. Introduction**

The culture is an essential factor in explaining international differences pointed out in the accounting literature. In studies, where are analyzed the differences between local and international standards, the authors emphasize that the culture turns out to be more explanatory than the legal system in explaining accounting differences and international harmonization (Ding, Jeanjean and Stolowy, 2005; Zeghal and Lahmar, 2016).

A country's cultural characteristics can be reflected in the accounting approach of the respective economy, from the point of view of the applied

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accounting treatment and also from users' requirements of the accounting information. In assessing the degree of difficulty existing in the adoption of IFRS by a country, it is important to analyze the accounting conclusions resulted from the culture of that particular country, based on dimensions and cultural values (Borker, 2012a)

The paper aim is to evaluate the impact of cultural dimensions on accounting in CEE countries concerning the adoption process of IFRS for SMEs. In achieving this aim, we identified the cultural characteristics of CEE countries using two basic models of cultural dimensions: the six dimensions of Hofstede (1980, 2010) and Gray's values (1988).

## **2. Literature review**

### **2.1. Hofstede's cultural dimensions model**

In order to identify the cultural characteristics specific to a society, but also to compare one country with another depending on the extent to which certain cutaneous characteristics are present, cultural dimensions are often used according to Hofstede's model.

Professor Geert Hofstede's model is recognized worldwide as the first empirical model on which the cultural dimensions of a nation can be measured. According to this model, in the initial version there were four cultural dimensions that could be evaluated among a society, and in 2001 another two dimensions will be added to the model, reaching a total of six cultural dimensions that can be measured in order to characterize a jurisdictions and its assessment compared to others.

Based on the Hofstede's model, were identified as six measurable cultural dimensions:

1. Power Distance - PDI
2. Uncertainty Avoidance - UA
3. Individualism versus Collectivism - IND
4. Masculinity versus Femininity - MAS
5. Long-Term Orientation - LTO
6. Indulgence versus Restraint - IVR

**Table 1. Hofstede's cultural dimensions model**

<b>Dimension</b>	<b>Meaning</b>
<b>Power Distance (PDI)</b>	PDI measures the degree of inequality in society. Also, defines the measurement to which the less powerful members of organisations and institutions within a country expect and accept that power is unequally distributed. The main idea of PDI is that individuals in an organised group are not equal, reflecting how the members perceive the inequality in a lower position.
<b>Uncertainty Avoidance (UA)</b>	UA can be defined as the measurement that the members of a culture feel vulnerable to unknown or ambiguous situations. Among other manifestations, this idea is expressed by predictability and by requirement for written and unwritten rules.
<b>Individualism versus Collectivism</b>	Individualism refers to cultures in which the bonds among people are unconstrained, everyone is expected to look on himself or herself and his or her family. The opposite of individualism, collectivism relates to cultures in which people from childbirth further are integrated into powerful groups, which during people's lifetime continue to defend them in return for absolute loyalty.
<b>Masculinity versus Femininity</b>	A culture is called masculine when are different: men are supposed to be assertive, sturdy and focused on material success, whereas women are supposed to be more modest, tender and concerned with the quality of life. A feminine culture is when affective gender roles overlap: both women and men are supposed to be modest, fragile, and worried about the their life quality.
<b>Long-Term Orientation (LTO)</b>	LTO promotes the values oriented toward future rewards, in particular, prudence and perseverance. Its opposite pole, short-term orientation, represents the development of attributes related to the past and present, especially respect for tradition and satisfying social obligations.
<b>Indulgence versus Restraint (IVR)</b>	Indulgence reflects an inclination for tolerate relatively free satisfaction of natural human desires related to enjoying life and having fun. Its opposite pole, restraint, reflects a belief that such gratification needs to be curbed and regulated by strict social norms.

Source: based on (Hofstede, Hofstede and Michael, 2010)

## **2.2. Gray's Accounting Values**

Having Hofstede's dimensions (1980), Gray (1988) put up four values and four hypotheses that could explain and predict the differences between countries' accounting practices according to their cultural dimensions. He argues that the culture is related to accounting operators' accounting systems and also, that the accounting is affected by the practices.

Gray (1988) introduces a framework extending the concepts of Hofstede's model of cultural patterns. His framework examines the development of accounting systems by using accountants' value systems, identifying four fundamental accounting values: professionalism versus statutory, uniformity versus flexibility, conservatism versus optimism and secrecy versus transparency.

**Table 2.** Gray's Accounting Values

<b>Values</b>	<b>Meaning</b>
<b>Professionalism versus Statutory</b>	an inclination for the use of individual professional beliefs and the maintenance of professional self-regulation as opposed to conformity with rigid legal requirements and statutory control.
<b>Uniformity versus Flexibility</b>	an inclination for the enforcement of homogeneous accounting practices between companies and the consistent use of such methods over time as opposed to flexibility by the perceived circumstances of individual companies.
<b>Conservatism versus Optimism</b>	an inclination for a prudent approach to measurement to manage with the uncertainty of future events as opposed to a more positive, risk-taking way.
<b>Secrecy versus Transparency</b>	an inclination for confidentiality and the restriction of disclosure of information about the business only to those who are closely involved with its management and financing as opposed to a more transparent, open and publicly accountable approach

Source: based on Gray (1988)

## **3. Research methodology**

The purpose of this paper is to evaluate the impact of cultural dimensions on accounting in CEE countries concerning the adoption process of IFRS for SMEs. In achieving this purpose, we identified the cultural

characteristics of CEE countries using two basic models of cultural dimensions: the six dimensions of Hofstede (1980, 2010) and Gray's values (1988). The sample selected was analysed for Hofstede's model and a similar accounting profile based on Gray's values. Further, we compared the profile of each jurisdiction to a favourable profile proposed by Borker (2012) for the adoption of IFRS.

We selected eleven CEE countries for the analysis: Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia. We will examine each country by Hofstede's six cultural dimensions and also by the values of Gray's framework. Profiles for each country will be compared to a favourable independent profile proposed as part of a broader analysis of cultural patterns, for IFRS for SMEs's successful adoption.

The paper's basis is the literature review in the field of CEE economies culture, IFRS features and means of implementation, while the data collected from several mentioned sources is analysed based on the personal judgement of the author, as well as by quoting various researchers on the corresponding areas.

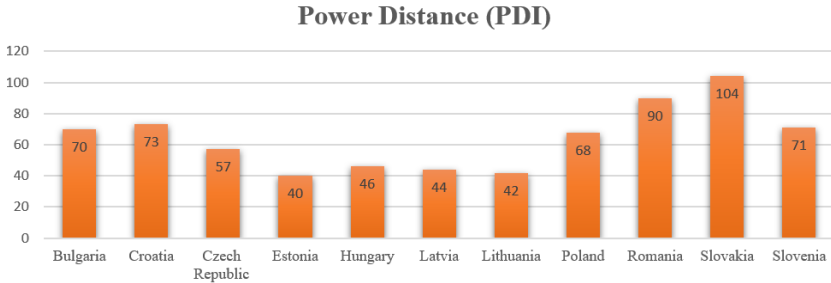
## **4. Analysis results**

### **4.1. Hofstede's Cultural Dimensions**

To analyse the CEE countries culture based on the six dimensions, the paper is using the data extracted from Hofstede's research, which provide the required scores for each dimension. The data is collected from the following source: Geert Hofstede, Gert Jan Hofstede, Michael Minkov – *Cultures and Organizations: Software of the Mind Revised and Extended 3rd Edition*, New York: McGraw-Hill, USA, 2010 and also is available on [www.geert-hofstede.com](http://www.geert-hofstede.com).

### 4.1.1. Power Distance (PDI)

**Chart 1. Power Distance (PDI) - Hofstede's cultural dimensions assessment for CEE countries**



(Source: data collected from <http://geert-hofstede.com/countries.html>)

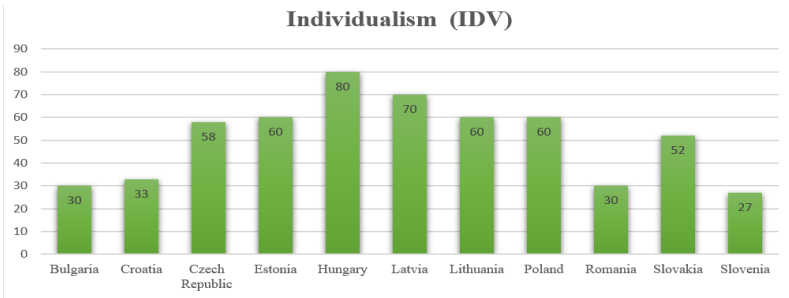
The lowest score on PDI dimension ranging from 40 to 46 (Estonia – 40, Hungary – 46, Latvia – 44 and Lithuania – 42) shows an inclination for equality, decentralisation of power and decision-making. In these countries, managers count on the experience of their team members, allowing them to express their opinions and disagreement, as well as to be included in the decision-making process. Employees expect to be consulted, based on direct and participative communication. They dislike control and attitude towards managers are informal and on a first name basis.

The other CEE countries had relatively high scores on PDI dimension ranging from 57 to 104 (Czech Republic – 57, Poland – 68, Bulgaria – 70, Slovenia – 71, Croatia – 73, Romania – 90 and Slovakia – 104). These high scores show that hierarchy is accepted in an organisation, reflecting inherent inequalities, where subordinates expect to be told what to do.

In countries scoring high on PDI (e.g. Slovakia – 104) it is entirely acceptable that some people had more power than others and expected that these people also use their power but not in a negative way, creating clarity and structure for people around them.

### 4.1.2. Individualism (IDV)

**Chart 2. Individualism (IDV) - Hofstede's cultural dimensions assessment for CEE countries**



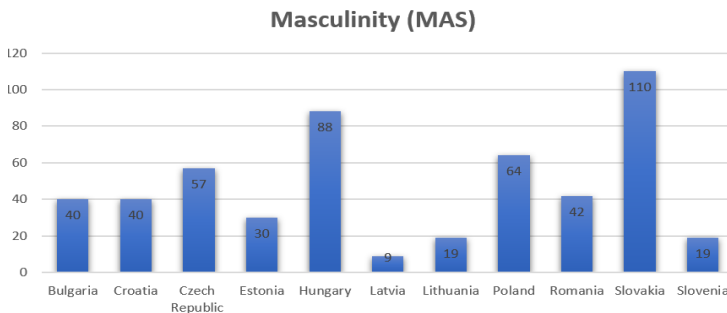
Source: data collected from <http://geert-hofstede.com/countries.html>

Bulgaria, Croatia, Romania and Slovenia have a low score on IDV ranging from 27 to 33, being considered countries with tendencies to collectivism, maintaining healthy relationships where everyone takes responsibility for fellow members of their group.

The highest scores on IDV ranges from 52 to 80. In these countries is a high preference for a social framework, where people are expected to take care of themselves and their immediate families only.

### 4.1.3. Masculinity (MAS)

**Chart 3. Masculinity (MAS) - Hofstede's cultural dimensions assessment for CEE countries**



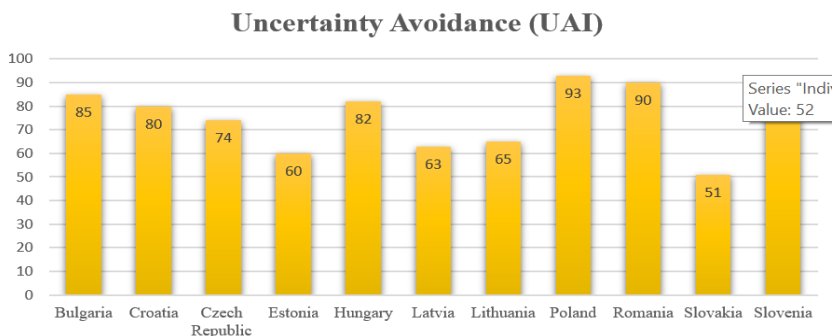
Source: data collected from <http://geert-hofstede.com/countries.html>

Seven countries from CEEC sample (Latvia – 9, Lithuania and Slovenia – 19, Estonia – 30, Bulgaria and Croatia – 40, Romania – 42) are considered feminist countries, where the people value equality, solidarity and quality of their lives. Others principal values of these countries are the tolerance towards the culture of other nations, and modesty, where communication is very diplomatic and soft.

The other four countries have a high score on MAS, ranging from 57 to 110. Czech Republic, Poland, Hungary and Slovakia are considered masculine countries, where it is imperative to be regarded as successful, reaching your goals and have high living standards.

#### 4.1.4. Uncertainty Avoidance (UAI)

Chart 4. Uncertainty Avoidance - Hofstede's cultural dimensions assessment for CEEC



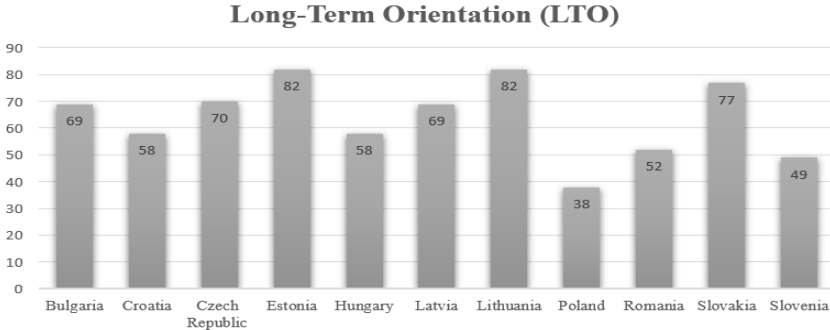
Source: data collected from <http://geert-hofstede.com/countries.html>

From our CEE countries sample, Slovakia shows no clear preference for UAI, scoring only 51 points. The other ten CEE countries sample incline for Uncertainty Avoidance, with scores from 60 to 92. In these countries exists an emotional need for rules, laws are adopted to avoid uncertainty, rigid codes of beliefs and behaviours are maintained, having a high intolerance of different practices and ideas



#### 4.1.5. Long-Term Orientation (LTO)

Chart 5. Long-Term Orientation - Hofstede's cultural dimensions assessment for CEEC



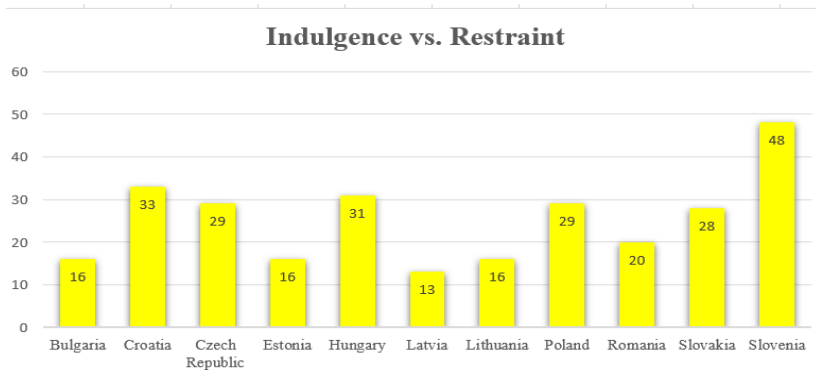
Source: data collected from <http://geert-hofstede.com/countries.html>

All the CEE countries sample except Poland (38) and Slovenia (49), incline to long-term orientation with scores ranging from 52 to 82, having a pragmatic orientation perspective. Poland and Slovenia are more normative in their thinking than pragmatic, concerning to establish the absolute truth. These two cultures have great respect for traditions and small focus in achieving fast results.

LTO dimension describes how each culture has to preserve some links with its past while handling the tests of the present and future. In these countries, people believe that the context, situation and time influence the truth. They have a great ability to adapt their traditions with no trouble to the changed circumstances and also great perseverance in achieving their goals.

#### **4.1.6. Indulgence vs Restraint (IVR)**

**Chart 6. Indulgence vs Restraint - Hofstede's cultural dimensions assessment for CEEC**



(Source: data collected from <http://geert-hofstede.com/countries.html>)

From our CEE countries sample, Slovenia shows no clear preference for this dimension, scoring only 48 points. The other countries incline to Restraint, with scores ranging from 13 to 33, tending to cynicism and pessimism. In this type of cultures exists perceptions that their actions are restrictive regarding social rules, reflecting a belief that human desires related to enjoying life and having fun need to be curbed and regulated.

#### **4.2. Gray's Accounting Values**

Gray's framework examined the development of accounting systems by using accountants' value systems, identifying four fundamental accounting values: professionalism versus statutory, uniformity versus flexibility, conservatism versus optimism and secrecy versus transparency. Gray suggests that these accounting values influence accounting systems.

In his paper, Gray proposes four hypotheses on the interaction between identified cultural characteristics and the development of accounting systems, the regulation of the accounting profession and perspectives towards financial management and disclosure.

Applying Gray's four hypotheses to the CEE countries sample, we have the following results:

**Table 3. Results of Gray's Framework**

<i>Countries</i>	<i>H1</i>	<i>H2</i>	<i>H3</i>	<i>H4</i>
<i>Bulgaria</i>	Statutory Control	Uniformity	Conservatism	Secrecy
<i>Croatia</i>	Statutory Control	Uniformity/ Flexibility	Conservatism	Secrecy
<i>Czech Republic</i>	Professionalism/ Statutory Control	Flexibility	Conservatism/ Optimism	Transparency
<i>Estonia</i>	Professionalism	Flexibility	Optimism	Transparency
<i>Hungary</i>	Professionalism	Flexibility	Optimism	Transparency
<i>Latvia</i>	Professionalism	Flexibility	Conservatism/ Optimism	Transparency
<i>Lithuania</i>	Professionalism	Uniformity	Conservatism/ Optimism	Transparency
<i>Poland</i>	Statutory control	Uniformity	Conservatism	Secrecy
<i>Romania</i>	Statutory control	Uniformity	Conservatism	Secrecy
<i>Slovakia</i>	Statutory control	Uniformity	Optimism	Secrecy/ Transparency
<i>Slovenia</i>	Statutory control	Flexibility	Conservatism	Secrecy

Source: adapted of Borker (2012b)

### **4.3. Results**

According to the literature, the developing countries adopt IFRS much easier because their culture is an Anglo-Saxon culture (Zeghal and Mhedhbi, 2006, Zehri and Chouaibi, 2013). The favourable IFRS profile is also one of Anglo-Saxon culture, because the accent is on the individual rather than on regulatory systems that force uniformity (Borker, 2012b).

Borker (2013) identified a profile that best suits the application of IFRS. Based on Hofstede's research results, IFRS profile is characterise by low level of power distance, high level of individualism, average to high level of masculinity, average to low level of uncertainty avoidance, low level of long-term orientation and high level of indulgence. We will use as a point of reference and comparison the following IFRS favourable profile Table 5.

**Table 4. IFRS Favourable Accounting Value Profile**

<i>Gray's hypotheses</i>	<i>IFRS Favourable Profile</i>
<b>H1</b>	Professionalism
<b>H2</b>	Flexibility
<b>H3</b>	Optimism
<b>H4</b>	Transparency

Source: based on Borker (2013)

To be able to analyse the trend of cultural dimensions among our sample, we have extrapolated the characteristics of the IFRS favourable profile to the IFRS for SMEs favourable profile. In doing so, each country profile was compared to an independent IFRS for SMEs favourable profile proposed.

Based on the four hypotheses of Gray's framework and the favourable profile of IFRS (Borker, 2012a), the following are hypothesised (Table 5)

**Table 5. Hypotheses - Gray's framework**

<b>Hypothesis</b>	<b>Description</b>
<b>H1</b>	The higher, a culture is ranking in terms of professionalism and the lower in terms of statutory control, the more likely the culture is to rank highly in terms of IFRS for SMEs adoption.
<b>H2</b>	The higher, a culture is ranking in terms of flexibility and the lower in terms of uniformity, the more likely the culture is to rank highly in terms of IFRS for SMEs adoption.
<b>H3</b>	The higher, a culture is ranking in terms of optimism and the lower in terms of conservatism, the more likely the culture is to rank highly in terms of IFRS for SMEs adoption.
<b>H4</b>	The higher, a culture is ranking in terms of transparency and the lower in terms of secrecy, the more likely a culture is to rank highly in terms of IFRS for SMEs adoption.

Source: based on (Borker, 2012a) and Marina (2019)

In terms of Hofstede's cultural dimensions, from the selected sample, only a few countries partially meet the characteristics of the IFRS favourable profile. These countries are Estonia, Hungary, Latvia, Lithuania and Poland.

Regarding Gray's accounting values, from these countries, only Estonia and Hungary corresponding to the IFRS favourable profile (Table 3).

## **5. Conclusions**

Following the analysis, based on the results of the analysed countries for each cultural dimension and for each associated accounting value, the following were obtained, namely Estonia and Hungary corresponding to the favourable IFRS for SMEs profile. Despite the results, none of these two countries applies IFRS standards for SMEs according to the *IFRS - Who uses IFRS Standards?* ([www.ifrs.org](http://www.ifrs.org)), but this analysis shows that the two countries are prepared and can easily accept the changes that could come with the implementation of IFRS for SMEs.

For an easy transition from the national accounting system to the IFRS for SMEs, each country must be prepared to have the necessary tools for accounting reporting, for management and suitably trained staff. Simultaneously, this transition must be carried out gradually, because professional accountants need sufficient time to understand the new concepts so that they can develop and establish their accounting judgment and apply these new concepts without any trouble (Marina, 2019).

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