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The impact of national influence on accounting estimates: Implications for international accounting standard-setters

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Abstract

The results of prior research suggest that national accounting systems are significantly associated with differences in market valuations and various other macromeasures. These results, however, rely heavily on the analysis of archival data or survey evidence directed at national system differences. As Pownall and Schipper [Accounting Horizons (1999) 259] note, archival research necessarily depends on the information in the financial reports and cannot explain the process linking the underlying standards to the reported information. This study examines this process by investigating judgments made by accountants in France, Germany, and the United States. To facilitate a comparison of this process across international boundaries, our experiment presents these accountants with the *same economic facts that are governed by similar financial reporting rules*. Our results indicate that, even given similar facts and rules, judgments among the three nations' accountants vary significantly. They also suggest that national culture interacts with findings accepted as general within behavioral decision research. © 2001 University of Illinois. All rights reserved.

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1. Introduction

Previous international financial reporting research has focused on developing an understanding of the different effects that national accounting *systems* have on firm valuation (e.g., Saudagaran & Meek, 1997; Tay & Parker, 1990; van der Tas, 1988). The general conclusion of this research is that different financial reporting systems have diverse effects on firm valuation. The purpose of this paper is to extend the current literature by investigating whether the factors associated with system differences tend to affect differences in individual accounting judgments when the accounting standards across countries are nearly identical. In contrast to the prior literature, our study focuses on the individual judgment of accountants who are faced with similar accounting standards. Thus, our study has the capability of addressing whether uniform accounting standards will result in comparable financial reporting across borders.² Our work is motivated by the decision of the Securities and Exchange Commission (SEC) to consider the implementation of uniform international accounting standards.

Several recent studies question the inferences that can be drawn from the prior literature due to limitations in the research designs employed (Gernon & Wallace, 1995; Pownall & Schipper, 1999; Prather & Rueschhoff, 1996; Saudagaran & Meek, 1997). For example, Pownall and Schipper (1999, p. 261) point out that archival studies necessarily depend on reported information and cannot detect differences that might arise in the process linking countries' standards and reported information. Specifically, they note that "existing research methods cannot in general distinguish the effects of standards from the effects of interpretation/application." Our primary objective is to address the concerns of Pownall and Schipper by investigating whether the financial reporting judgments made by accountants in different nations are consistent when those accountants are faced with the same economic facts and similar financial reporting standards. Thus, our study addresses the issue of the cross-border effects of "interpretation/application" on financial reporting.

² The issue under consideration is whether consistent standards [such as those being considered by the International Accounting Standards Committee (IASC)] are being interpreted consistently across international boundaries. The IASC will develop consistent standards with the objective of achieving comparable financial reporting across countries. This will only be achieved if the standards are applied consistently across countries. While we are not examining the application of an "international accounting standard," we are examining a consistent standard across these countries, which is the objective of the IASC. SFAS 5 (FASB, 1975) governs the accounting for warranty expense in the United States. According to SFAS 5, the estimated amount of warranty expense should be charged to income if the following two conditions are met: (1) on the balance sheet date, it is probable, from information available before the release of the financial reports, that the entity has incurred a liability, and (2) the entity can reasonably estimate the amount of the warrant expense. Afterman (1995) indicates that the accounting rules governing the recognition of contingent losses in France and Germany are similar to those in the United States. That is, all three countries require the accrual of likely (probable) contingent losses. Further, the accounting for contingent losses in all three countries is subject to relatively broad guidance, which is generally characteristic of international accounting standards. Brackner (1985) expresses concern over the diversity that exists in the application of SFAS 5 with respect to the estimation of future events or probabilities. This same issue is addressed by Afterman (p. B10.04) when he indicates that contingent loss accruals are subject to manipulation for the purpose of income smoothing in France and Germany.

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