

# [The impact of culture on conservatism](https://assignbuster.com/the-impact-of-culture-on-conservatism/)

Discuss the implication for the global harmonization of financial reporting standards raised by gray’s model? If cultural values affect the development of financial reporting rules, and countries differ with respect to cultural values, then financial reporting rules will differ across countries. If financial reporting rules are strongly influenced by culture and cultural values do not change significantly over time, culture acts as an impediment to reducing differences in financial reporting rules that exist across countries.

Discuss the implication this argument has for the comparability of financial statements across countries, even in an environment of international accounting harmonization. Identify areas, which differences in cultural dimensions across countries could lead to difference in the application of financial reporting rules? Even if all countries agreed to use the same financial reporting standards (harmonization), to the extent that application of those standards involves judgment, cultural differences could lead to differences in the application of those standards.

For example, in applying a rule that requires recognition of a contingent loss when its realization is “ probable,” accountants in more highly conservative countries might err on the side of conservatism by establishing a lower probability threshold than would accountants in less conservative countries. Other areas in which culture might lead to differences in the application of financial reporting rules include areas in which estimation and judgment are involved: warranty expense, bad debt expense, revenue recognition, asset impairment tests, obsolete inventories, etc.

Discuss the implications that the model presented in part II of this case has for the internal auditors of Cancan Enterprises in carrying out their responsibilities. Cancan’s internal auditors need to be aware that accountants in these different countries might have culturally-determined biases in the way that they apply the company’s accounting policies. Accountants in Brazil and Korea are likely to be more conservative (higher UA, lower IND) in applying Cancan’s accounting policies than the accountant in Sweden (lower UA, higher IND).

The internal auditor needs to plan to conduct tests to determine whether this bias is operating. Contingencies, warranty expense, bad debt expense, revenue recognition, asset impairment tests, and obsolete inventories are all areas that require considerable judgment. In addition, the accountants in Brazil and Korea may be less willing to provide information requested by the internal auditors because of a higher level of secrecy.