

DIFFERENCES AND THE FACTORS OF CONVERGENCE OF MANAGEMENT ACCOUNTING SYSTEMS IN DEVELOPED AND LESS DEVELOPED COUNTRIES

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ABSTRACT

The article focuses on two areas. First part examines the major differences amongst the systems in developed and less developed countries and the rational behind it i.e. inadequate financial resources, weak business structure, poverty, political influence, weak state institutions, difference in taxation and social-economic factors. The second part examines the factors which are motivating and intimidating these two sets of groups to follow the similar management accounting practices i.e. discouraging the system of protection, innovation in IS/IT technologies, normative & mimetic aspect, international strategic alliance and international trade agreements. Organizations operating in LDC's need to understand the pros and cons of each management accounting system considering local as well as international environment before adaptation. There are number of factors which a company needs to confront with like international collaboration, international competition, taxation, socio-ethical issues, technology, political conditions etc. Therefore the companies need to adopt the system which suits the most considering current and future prospects. However the converging factors are seen more active and dominating therefore in coming few years there are more expectation to have similar set of standards of management accounting systems.

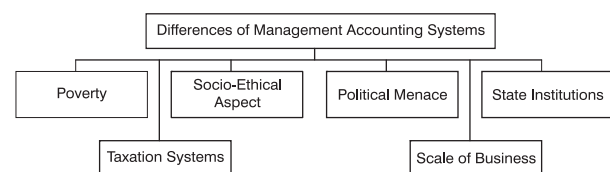
1. INTRODUCTION

According to World Bank, the countries, where the gross income of an individual is lower than \$9,266 per annum are classified as less developed countries (LDC's) or underdeveloped countries. Management Accounting Systems (MAS) in developing countries may operate differently from those in developed countries (Hopper et al. 2003). It is a valid argument in a way that most of the LDC's have adopted the systems from the developed countries but were unable to take the true benefits claimed and associated with them therefore the desired is to probe the critical factors which become the major ingredients for such failure. The paper is divided in two parts. First part examines the major differences among systems in developed and LDC's and the rational behind it. The second part of the paper looks toward factors which are motivating these two set of groups (developed and LDC's) to follow the similar management accounting practices. The significance of the paper is especially from LDC's point of view i.e. to understand their need to adopt management accounting tools and practices considering local and international requirement and the other motivating factors which they need to underlay before switching to any new MAS.

2. DIFFERENCES OF MANAGEMENT ACCOUNTING SYSTEMS

Most of the LDC's (India, Pakistan, China, Korea, Malaysia etc) after having independence pursued mod-

ernization and the foot steps of modern civilization through following central state planning and governmental control of the large enterprises (Hopper et al. 2003). The reason for such control is obvious for not having enough financial resources and business structures to support individually. The systems which LDC's have adopted were mostly from developed countries, typically based on computer technology to achieve operational excellence (which is the main theme of adopting automated computer technologies). Other than that another main accounting system, which LDC's have adopted is the budgeting system to keep in control the expenses of the private and public sectors (Pakistan and Indian public departments are the live examples of expense based budgeting systems). The following are number of factors influencing organizations in LDC's for management accounting practices:



2.1 Poverty:

The poverty is a major factor towards difference in adoption of management accounting tools and techniques. Most of the companies in LDC's do not have enough resources to safeguard themselves by having

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various management accounting tools like insurance against unwanted circumstances (natural disasters, theft), inventory buffers (protection against unexpected business transactions), and improvised information systems (to achieve operational and competitive excellence). This lack of appropriate management accounting tools, leave managers with no other choice to take decisions in a traditional way, without considering the market forecasts and competition. In such environment accounting is seen nothing more than a clerical job, just as book keeping. In developed countries the theme of the management accounting system has been changed enormously, where accountants can be seen as a part of the strategic alliance of the firm, and the managers should understand the strategic role of accounting system (Steadman et al. 1995).

2.2 Socio-ethical aspect:

Due to lack of capitalists, normally people in LDC's conduct business based on personal relationships or at family terms, which is a very conservative approach towards outside world. This approach is one of the major barriers towards adoption of new methodologies because the company gets estranged from various personnel traits and new emerging talent. Considering the developed countries, now there is almost a multicultural environment in every small to large size organization. In developed countries these methods work properly due to harmony under government strict regulations.

The literacy and experience level also matters a lot. It ensures the exposure to think and broaden the vision to evaluate what is best in the interest. We can't exercise any kind of modern MAS or policy till then the effective person would be in a position to properly grasp the main theme behind it. To properly run the modern MAS the organizations needs the right exposure to international environment and excellence in previous accounting tools like Japanese organizations, which most of the companies in LDC's don't have.

2.3 Political Menace:

Most of the countries from LDC's have weak political structure and are still trap in the black hole of dirty politics. In LDC's the politicians have much influence on business community due to their unwanted interests in different business sectors. This fact is also supported by Al-Eryani (1987) by stating that even the multinational corporations give special attention for having good relations with ruling government in LDC's. Therefore the relationship of business community with ruling politicians gets more importance than the business relations (Hopper et al. 2003).

2.4 State Institutions:

Also their have been noticed a lack of appropriate state institutions and other legislative agencies in LDC's due to which they often have a problem of swings in

currency fluctuation, commodity prices and other relative issues. In LDC's often there is an environment of uncertainty and risk, which leads to wrong market forecasts, and the remaining is catalyzed by insufficient information systems, which provides less security to creditors and investors. Often there has been evidence of poor financial reporting and taxation due to which several cases of bank frauds and companies defaulted at repayments and some later on (Hopper et al. 2003).

2.5 Taxation System:

According to Blake et al. (2003) the taxation rules have a deep influence on the financial accounting in all countries. We do believe that in a country, the taxation system can have an impact on MAS. The management accountants are free to take their own approach to cost allocation issues considering their tax requirements. For example; in Finland tax law requires the stock valuation on variable cost bases. This has been influential in promoting variable costing in the management accounts. From this we can have a very good idea about the major difference in cost allocation amongst developed and LDC's. Usually in UK the corporate tax rate (31%) is far more than eastern countries, this allows different mode of tax treatment in accounting according to different countries. The Chinese government wants foreign investment enterprises to exercise market based cost to secure the interest of local partner from foreign investors (Chan & Lo. 2004), which leads to different taxation treatment in accounts.

2.6 Scale of Business:

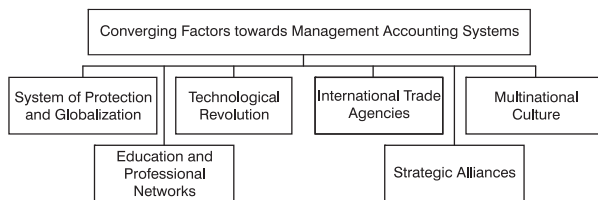
Most of the organizations in LDC's are at the stage of value chain, where they are trying to achieve the production and operational excellence through automation and by achieving the optimum level at economies of scale (where the benefits can't be capitalized further). Whereas in developed countries most of the large enterprises have already achieved the optimum level (Toyota, BMW, Ford, SONY, GM) therefore to create the margin beyond, they have to adopt the other methods like Just in Time (JIT) in collaboration with Kaizen and then eventually to other systems like activity based costing (ABC) and target costing (TC). The LDC's still have the same old internal approach that first to develop a product and deliver it with considerable margin (push approach), and not from the customer needs perspective or claimed benefits. In a way this approach of LDC's is right because of poverty, where demands of the claimed benefits (associated with the product) are always higher than the supply side, and also the customers don't have the enough financial resources to avail the respective commodity. So in such a situation enterprises usually work on value chain to remove the duplicate process and redundant the over staff to increase profitability (Low wages to temporary and subcontracted workers who were afforded little protection under industrialized relations law). Other than that with reference to

JIT (production where companies usually have kaizen rule by having the same level of quality), in LDC's companies also compromise on quality of products to reduce the cost as minimum as possible (Schmelze et al, Kato, 1993). Normally the government appears to be the central body of control but because of too much political intervention and cultural pressures it becomes almost impossible for the government bodies to properly regulate the policies regarding material, product pricing and other similar issues.

Other than that there are also some other issues like national legislation, religion, corporate cultures etc which could be the main reason for adoption of different MAS practices in LDC's.

3. CONVERGING FACTORS TOWARDS MANAGEMENT ACCOUNTING SYSTEMS

Instead of such a big cultural and ethnic differences between developed and LDC's, also there are several motivating and intimidating factors which are working towards MAS's convergence. This section will discuss the factors of convergence of management accounting in detail.



System of Protection and Globalization:

Amat et al. (1994) see the end of the system of protection that had shielded Spanish industry from international competition till the mid of 1970's as a major force for the development of MAS's in Spain. Recently the deregulation of Chinese and Indian markets catches the eyes of big foreign investors. Also the deregulation of banking and telecom sector in Pakistan has seen enormous development. These markets are now become more attractive for investments. Other than that the competitive pressures of a global economy are cited by Bhimani (1996) to explain growing interest in advance management accounting techniques in both Germany and Italy.

Similarly the concept of globalization infuses the whole new life in the international business. Now the companies' territories are no more restricted to some specific geographical areas. The whole world is now in direct competition with each other and converted into a kind of global village, where everyone is trying to give the best and using the top leading quality tools to get the competitive edge (transfer pricing is too common in case of china and India refer to Chan & Lo (2004), similarly target costing in Japan). In Brazil it has been noticed that the industries had led the way in developing the

innovative approaches to costing have been those which do not enjoy government protection (Bhimani, 1996) (like in Pakistan the motorcar, textile, and airline industry is protected by government).

3.1 Technological Revolution:

The remaining difference is evolved by the fast moving and innovating IS/IT technologies, which are coming in a form of standard and customizable software's based on the leading management tools and concepts. Here I would like to mention the name of SAP application, which is based on International accounting standards. It is one of the fastest emerging application systems for enterprise resource planning (ERP). Recently most of the companies in the east are thinking to adopt this system to coherent their process and methods to western leading enterprises (mimetic pressure as identified by Lukka & Grunland (1998)). Therefore around the globe companies are now trying to adopt the leading MAS like JIT, ABC, Target costing etc to reduce the cost and to achieve the competitive edge by adopting different generic strategies (Porters, 1985 this idea is also getting vague due to globalization. Now most of the companies are having a mix of strategies e.g. Boeing, P&G, Toyota etc).

3.2 International Trade Agencies:

There are also the involvements of some coercive pressures, which are contributing towards the convergence of MAS's. Due to the recent development in 21's century i.e. WTO and other transnational trade agreement like SAFTA, NAFTA etc enforces all the member countries to follow the same kind of trade laws and procedures. This allowed the companies from different territories to come together and trade according to international set standards. For example the letter of credit (LC) is normally used instrument in international trade. Now the banks usually follow the same set of policies and regulations to avoid the trade agreements conflicts. Agreement terms can be different at national level due to cultural, religious and other ethical reasons but at the international level they usually have the similar kind of terms and regulations for the standardization purpose.

3.3 Multinational Culture:

The multinational structure and the culture of the mega organizations like Airbus, Boeing, Proctor & Gamble, Toyota, Honda and Unilever etc also demands for the standardization of systems. Multinational organizations emphasis the need for the use of similar kind of accounting tools to all their subsidiaries, this reduces the problem of information integration and system synchronization. Other than that international financial reporting standard (IFRS) also enforces the listed companies to follow the set standard accounting procedures to stop malfunctioning and frauds at external reporting level and secure the confidence of shareholders and other external stakeholders. Other reason being to generate

financial reports in a standardize format (IFRS) is to make them understandable to international investors.

3.4 Standardize Education and Professional Networks:

From the normative aspect, the recent trends of professionalization of management accountants (consultants) have included the promotion of the similar ideas of cost management (ABC, Target costing etc) and other financial measures such as balance score card, critical success factor etc (Granlund & Lukka, 1998), which are acting as a major contributing factor towards the convergence and implications of the similar management accounting systems. Most of the companies having foreign investment in LDC's are adopting new management accounting tools to acclimatize with new technologies and processes without understanding the business demands.

DiMaggio & Powell (1983) suggested that the two major sources of convergence are; the professional networks and the university education. In universities the similar books and the case studies leads to the similar kind of new emerging management thinking. Other than that the recent educational revolution in eastern world influenced thousands of students from LDC's to study in western universities, this will have a major contribution towards the convergence of management accounting as they will have a similar education background. According to Blake et al (2003) "in the absence of management accounting professional bodies the role of accountancy used to be filled by four ways i.e. 1) trained public auditors and accountants may move into the management accountants role e.g. Institute of chartered accountants of England and Wales (ICAEW) and French Ordre des experts comptables et comptables Agrées (OECCA), 2) voluntary bodies may emerge to discuss the accounting issues like The Spanish Association of Accounting and Business Administration (AECA), 3) engineers may become involve in management issues like in France where the detailed costing provisions in the accounting plan has emerged, under the influence of engineers, the concept of the 'Tableau de Bord', literally an instrument panel, presenting key physical and financial indicators, 4) universities and consulting firms can be important channel for the circulation of management accounting ideas like Belgium". But now due to the international accounting bodies like IFRS and other major national institutes like CIMA in the UK, IMA in US and AECA in Spain as mentioned before are working more closely to regulate the international standards at macro level. There are still some major cultural and corporate issues which are not yet resolved at micro or national level, which are one of the major sources for divergence in small and medium size enterprises (SME).

3.5 Strategic Alliance:

Last but not the least the emerging issue which is contributing heavily towards the convergence of management accounting system is the international strategic alliance (ISA). This tool is not new but the use of it is more common since the last three decades. We have seen a number of large business giants coming together for the same market stake and to get the competitive advantage over their traditional rivals and new emerging challengers (Lorange & Roos, 1991). For-example Sony-Ericsson, HP-Compaq, Toyota-Frontier, Atlas-Honda, and LG etc. Usually companies exercise this tool, when the market gets too saturated and the pace remains the only key to get the competitive advantage. There are also other reasons and benefits associated with the ISA like synergy; getting access to far reach markets, protectionism, experience, competences etc (refer to case study of American and British Law firms Mellahi et al. 2005). As our discussion is related to management accounting system, I feel the joint ventures and alliances increases the need for having the similar kind of management accounting system so that the entire participants can easily integrate the results and systems with their parent company. In the near future we will come to see the major alliances amongst major giants, which will enhance to increase the need for the use of same accounting systems.

4. CONCLUSION

Examining the differences of management accounting systems amongst the developed and LDC's and their implications according to different socio-economic factors, it can be stated as, these factors would become less important and will be discouraged in the future because of growing international business collaboration, but still, there would be some socio-ethical factors remains, which would contribute towards the divergence of some of the management accounting treatments and systems. The converging factors like globalization, standardized application softwares like SAP, international trade agencies (WTO, SAFTA, NAFTA etc), and other accounting and operating standards like IFRS, would get more regulated and will have more implications eventually. This will enforce the globally accepted set standards and systems in all countries whether they are developed or not. In coming few years we would expecting to have similar set of standards of management accounting systems which will not only enhance the organization ability to understand international environment but also help them to learn the key strategic tools from developed nations. The conclusive statement for organizations operating in LDC's is that they need to understand the importance of each management accounting tool considering local as well as international environment before adaptation. There are number of factors which a company needs to confront with like international collaboration, international competition, taxation, socio-ethical issues, technology, political conditions

etc. Therefore the companies need to adopt the system which suits the most considering current and future requirements.

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