THE INFLUENCE OF GLOBAL FINANCIAL CRISIS ON THE ACCOUNTING POLICIES

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Accounting practices are deeply implicated in the current financial crisis and in proposals for recapitalizing financial institutions and restoring stability to the global financial system. Noting that very little research has been done on the accounting policies implications of such crises, particular consideration is given to exploring the significance of and potential for research on this topic. This article discusses the changes that occur in the accounting policies starting with 2007 when the economic catastrophe begins. The empirical results suggest that companies introduced new components on their accounting policies with the emergence of financial crisis and there isn't a trend of changes in accounting policies depending on the activity of a company.

Keywords: Accounting policies, economic-financial crisis, financial statements, management decisions

JEL Classification: M41 – Accounting

1. INTRODUCTION

While it has become common place to blame bankers and their bonuses for the current global financial crisis, as the economic ruin deepens and spreads more fundamental questions will undoubtedly be asked about our economic system and the institutions upon which it is founded. The magnitude of this financial and economic crisis calls for a fundamental reassessment of all areas of business and economic scholarship, including accounting research.

The current economic and financial crisis has significant implications for accounting, both for practice and for the research community. In the areas of financial accounting, auditing, management accounting and the regulatory institutions that oversee accounting and auditing practices there are genuine worries that the crisis has revealed numerous problems and inadequacies.

There is a sample of companies that have already responded to the requirements of changing the components of the accounting policies caused by the current economic environment, this is the reason why we consider a study to quantify and analyze the changes in accounting policies.

2. RESEARCH METHODOLOGY

The importance of having accounting policies well presented and the relation between costs and benefits trigger the interest of all the professionals in this field. In the qualitative stage, in order to deepen the knowledge of this theme, we used the method of documentation, through rigorous analysis of the specialized literature, the international regulations (IAS 8 and IFRS with direct implication into the accounting policies). Based on our findings we try to establish a trend in terms of accounting policies for 23 entities listed on the New York Stock Exchange.

3. LITERATURE REVIEW

The world of accounting practice is implicated in the current financial crisis in a number of ways. The most obvious is through financial reporting requirements governing asset valuation and off-balance sheet entities (Ryan, 2008). The importance of these seemingly mundane accounting rules is underscored by the fact that the solvency and survival of our major financial institutions now turns on how accountants value bank assets and the extent to which auditors require firms to consolidate off-balance sheet entities.

The number reported on the various financial statements provide important information to decision makers, but most users require additional details to facilitate their analysis. All financial reports include additional information in notes that follow the statements.

The first note is typically a summary of significant accounting policies. The summary of significant accounting policies tells the user which accounting methods have been adopted by the company. It is impossible to analyze a company's financial results effectively without first understanding the various accounting methods that have been used. It would be similar to discussing a swimmer's time in the 100 freestyle without knowing if the race had been measured in yard or meters. (Short D., 2003)

PricewaterhouseCoopers and KPMG have been conducted a study, in 2009, regarding the significant accounting policy disclosures and the result of their research is summarized above:

- PwC noted that information around the decision to consolidate (or not) was largely inadequate. For many of the banks surveyed they found that the significant accounting policy disclosures surrounding SPEs failed to provide a tailored discussion of the specific policies. Quite often, disclosures took the form of a repetition of the wording in the consolidation standards. Of the banks surveyed, 20 disclosed securitization activity as well as their accounting policies surrounding derecognition. However most of the banks provided only a brief repetition of the derecognition standard as opposed to providing a tailored discussion of the judgments made in applying accounting policies.
- KPMG figures that 9 banks provided a detailed description of their accounting policy in relation to the consolidation of SPEs. Only 6 banks provided detailed descriptions of the reasons for not consolidating some vehicles, or the nature of changes that led them to consolidation.

Accountants inevitably make many accounting estimates and policy decisions when preparing financial statements. They must select depreciable lives for long-lived assets choose: inventory costing method, make assumptions about pensions, and make many more judgments. These accounting estimates are driven by an entity's accounting policy as it applies to the issues at hand. These decisions could significantly affect a company's financial statements and how users understand a company's results and financial position. (Holtzman M., 2007)

Financial statements must be clear and understandable. They are based on accounting policies which vary from enterprise to enterprise, both within a single country and among countries. Disclosure of the significant accounting policies on which the financial statements are based is therefore necessary so that they may be properly understood. (International Accounting Standards No. 1, paragraph 10)

Accounting standard setters argue that information about the accounting policies used by a reporting entity is essential for financial statement users in interpreting financial statements. (Hope O., 2007)

4. QUALITATIVE ANALYSIS OF REGULATIONS REGARDING THE ACCOUNTING POLICIES

IAS 8 Accounting policies, changes in accounting estimates and errors is the international regulation which prescribe the criteria for selecting and changing accounting policies, together with the accounting treatment and disclosure of changes in accounting policies, changes in accounting estimates and corrections of errors. The Standard is intended to enhance the relevance and reliability of an entity's financial statements, and the comparability of those financial statements over time and with the financial statements of other entities.

Accounting policies are the specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements. When an IFRS specifically applies to a transaction, other event or condition, the accounting policy or policies applied to that item shall

be determined by applying the IFRS and considering any relevant Implementation Guidance issued by the IASB for the IFRS.
IFRSs set out accounting policies that the IASB has concluded result in financial statements containing relevant and reliable information about the transactions, other events and conditions to which they apply. Those policies need not be applied when the effect of applying them is immaterial. However, it is inappropriate to make, or leave uncorrected, immaterial departures from IFRSs to achieve a particular presentation of an entity's financial position, financial performance or cash flows.
An entity shall select and apply its accounting policies consistently for similar transactions, other events and conditions, unless an IFRS specifically requires or permits categorization of items for which different policies may be appropriate. If an IFRS requires or permits such categorization, an appropriate accounting policy shall be selected and applied consistently to each category. An entity shall change an accounting policy only if the change:
(a) is required by an IFRS; or
(b) results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows. (Technical Summary of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, IASB , 01.01.2009)
From a substantive viewpoint relating to IFRS, this is so in that addressing global business changes that are uncertain, uneven, ongoing and evolving requires the application of judgment in assessing financial performance and position beyond mere reliance on the application of pre-defined rules.

5. QUANTITATIVE ANALYSIS REGARDING THE ACCOUNTING POLICIES CHANGES

Based on theoretical considerations and previous empirical research we developed a series of hypotheses that link the company's accounting policies changes caused by the current crisis. Quantitative research methodology initiate with choosing the investigated population. In this respect we have consulted the website of the New York Stock Exchange to identify the entities that have a major role in the international economy, and we choose those companies which were most active on the financial market from NYSE. To form a representative sample we have chosen 25 companies listed, but only 23 of companies have remained in our analyze because 2 of them haven't published on their website the financial statements for year 2006. In addition, each company from our sample is relevant and representative for the sector in which it is operating, and financial data is available to the general public as proof that we were able to achieve their financial reports for years 2006 (before financial crisis), 2007 (the year when financial crises arise) and 2008 (the second year of financial crisis), by accessing their website.
After analyzing the information that entities provided on their website, regarding changes in accounting policies caused by the current crisis, we developed 2 hypotheses that we considered relevant to our investigation:
H1: Companies introduced new components on their accounting policies with the emergence of financial crisis.
In an accounting context, materiality refers to the relative importance or significance of an item to an informed decision maker. An item or event is material if it is probable that the judgment of a reasonable person, relying on that information, would have been changed or influenced by its omission or misstatement. Many decisions regarding materiality call for the careful application of the accountant's judgment. The application of materiality often depends on the size of the particular item in relation to the overall size of firm. Obviously, what is material to Smith's Shoe Store is not material to General Motors. (Flamholtz. E., Diamond M., Flamholtz D.). Taking this into consideration, our research do not intend to compare the number of components of

accounting polices from one company to another, it intends to compare the evolution of components of accounting policies for each company over 3 years.

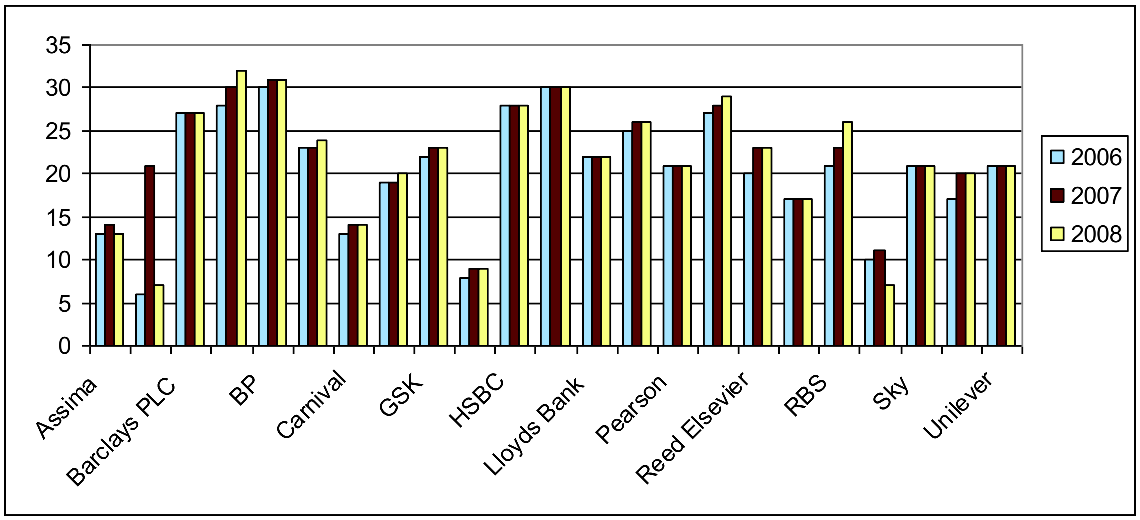
H2: There is a trend of changes in accounting policies depending on the activity of a company.

Astami E. concludes in her research that companies which belong to the same industry are directed towards the same direction when it comes to change their accounting policies.

6. RESULTS

We can state that all companies have been modified their accounting policies after the financial crash, 15 companies, out of 23, have been introduced new components on their accounting policies, which means that the managers considered the new economic environment a reason for introducing new elements in the financial statements.

FIGURE 1. COMPONENTS OF ACCOUNTING POLICIES CHANGES



Source: Compiled by author

Taking into consideration the above table we can not conclude that there is a trend of changes in accounting policies depending on the activity of a company and we believe that this occurs because our research have been done on a few number of companies.

TABLE 1. COMPONENTS OF ACCOUNTING POLICIES CHANGES TAKING INTO ACCOUNT THE ACTIVITY

Activity	**2006**	**2007**	**2008**
IT	13	14	13
Pharmaceutical	6	21	7
Financial services	27	27	27
Industry - natural resources	28	30	32
Industry - oil	30	31	31
Confectionery	23	23	24
Tourism	13	14	14
Drinks	19	19	20
Pharmaceutical	22	23	23
Construction	8	9	9
Financial services	28	28	28
Tourism, hotels	30	30	30
Financial services	22	22	22

Activity	2006	2007	2008
Industry - energy	25	26	26
Education	21	21	21
Insurance	27	28	29
Science and medical information	20	23	23
Industry - natural resources	17	17	17
Financial services	21	23	26
Construction	10	11	7
Media	21	21	21
Industry - automotive	17	20	20
Industry - food	21	21	21

Source: Compiled by author

7. CONCLUSION

The crisis, thus, challenges us to re-evaluate our research agendas – and perhaps also the institutional incentives and unexamined assumptions that drive them – so that accounting research can contribute to a broader social and political analysis of the financial crisis.

Financial reporting standards that are seen to adapt to the role of mitigating the risks of interpreting the increasingly complex global business environment and which find legitimacy on the grounds of both market imperatives and political and institutional alignment, will potentially achieve a sustained global presence in the future. If companies use a range of different accounting methods, stock market participants may have to devote considerably more resources to analyzing and comparing the companies' financial statements.

As a summary of our research we can state that for 23 listed companies from New York Stock Exchange only one hypothesis was accepted and this leads us to affirm that:

1. companies introduced new components on their accounting policies with the emergence of financial crisis; and
2. there isn't a trend of changes in accounting policies depending on the activity of a company.

With today's business environment of complex transactions and the recent crop of complicated accounting standards on derivatives, business combinations, stock-option compensation, postretirement benefits and income taxes, it is more difficult than ever to understand how underlying uncertainties affect the financial statements. New disclosures about accounting policies are supposed to meet this need. Thus, the paper adds both to the literatures on accounting policies changes of analysts' forecasts and to the international accounting literature.

Finally, it is important to recognize that accounting rules and changes in them are shaped by political processes (like any other regulation). The role of the political forces further complicates the analysis. For instance, it is possible that changing the accounting rules in a crisis as a result of political pressures leads to worse outcomes than sticking to a particular regime (e.g., Brunnermeier et al., 2009Brunnermeier et al., 2009). In this regard, the intense lobbying and political interference with the standard setting process during the current crisis provide a fertile ground for further study.

A useful direction for further research would be to increase the number of companies upon which we would do the research and also to introduce new variables that would quantify the reasons which determines the management to changes the accounting policies and if those changes are reliable for the company.

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