

THE ACCOUNTING IMPLICATION OF CULTURAL DIMENSIONS ON FINANCIAL REPORTING: A STUDY OF SELECTED MANUFACTURING COMPANIES IN NIGERIA

ARZIZEH TIESIEH TAPANG, PETER KEKUNG BESSONG AND CHARLES EFFIONG

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ABSTRACT

This study extends the literature on the impact of cultural dimensions on financial reporting practice and disclosure patterns of selected manufacturing companies in Nigeria by investigating the extent to which cultural dimensions (i.e. power distance, uncertainty avoidance, individualism and masculinity) influences financial reporting (mirrored by professionalism, uniformity, conservatism and secrecy). These cultural dimensions have served as a basis for a number of risks of material misstatements in the financial reporting process and an impediment to reducing differences in financial reporting rules that exist across countries. The study adopted a survey research design and data were collected by the use of questionnaires and analyzed using the ordinary least square (OLS) method. The results from the test of hypotheses revealed that financial reporting is significantly influenced by cultural dimensions. Finally, the study recommended that since accounting practice and financial reporting to a large extent is a product of its environment, there should be a direct link between cultural dimensions and financial reporting as it is potentially useful for users of accounting information because this provides them with supplementary information on the likelihood of material errors in financial statements.

KEYWORDS: Power Distance, Uncertainty Avoidance, Individualism, Masculinity

1.0 INTRODUCTION

1.1 Background of the study

The theory of cultural differences advanced by Hofstede (1980) and refined by House, Hanges, Javidan, Dorfman, and Gupta (2004), posits that cultural differences have significant effects on the development and operations of various professional practices, including accounting and external auditing. Cultural settings had been proposed by Hofstede (1980 and 1983) based on four cultural dimensions of power distance, uncertainty avoidance, individualism and masculinity. The study extends this line of research by

investigating the relationship between various cultural dimensions and professionalism, uniformity, conservatism and secrecy in financial reporting practice worldwide.

The primary objective of financial reporting is to provide high-quality financial reporting information concerning economic entities, primarily financial in nature, useful for economic decision making (FASB, 1999; IASB, 2008). Providing high quality financial reporting information is important because it will positively influence capital providers, investors, government, customers and other stakeholders in making investment, credit, and similar resource allocation decisions enhancing overall market efficiency (IASB, 2008).

Arzizeh Tiesieh Tapang, Department of Accounting, Faculty of Management Sciences, University of Calabar, P.M.B. 1115, Calabar, Cross River State, Nigeria.

Peter Kekung Bessong, Department of Accounting, Faculty of Management Sciences, University of Calabar, P.M.B. 1115, Calabar, Cross River State, Nigeria.

Charles Effiong, Department of Accounting, Faculty of Management Sciences, University of Calabar, P.M.B. 1115, Calabar, Cross River State, Nigeria.

Cultural values affect the development of financial reporting rules and countries differ with respect to cultural values, therefore financial reporting will differ significantly across countries. Gray (1988) extends Hofstede's model by overlaying accounting values and systems and their links to societal values and institutional norms. Gray argues that shared cultural values within a country lead to shared accounting values, which in turn influences the nature of a nation's accounting and financial reporting systems (Doupnik & Tsakumis, 2004).

1.2 Statement of the problem

Today, corruption remains a serious social problem, which is manifested in both advanced and developing countries. In the latter countries like Nigeria however, due to its endemic nature, it creates and fosters immense distortions in various institutional processes as a result of inherent erosion of essential checks and balances. Inadequacy of checks and balances will reduce the effectiveness and efficiencies in detecting material misstatement in financial statements.

Culture is an important environmental factor influencing financial reporting, accounting practices and management control systems. For example, a cross-cultural study suggests that people from different cultural backgrounds have different preferences for management practices and accounting control system.

These cultural dimensions (power distance, individualism, uncertainty avoidance and masculinity) are identified as dimensions that relate closely to factors affecting financial reporting in accounting population. These cultural dimensions have served as a basis for a number of risks of material misstatement in the financial reporting process.

Lastly, linking culture directly to financial reporting is potentially useful to users of accounting information because this provides them with supplementary information on the likelihood of material errors in financial statements.

1.3 Objectives of the study

The main objective of the study is to ascertain the accounting implication of cultural dimension on financial reporting.

The specific objectives of the study are as follows:

1. To ascertain the impact of power distance on financial reporting.

2. To investigate the relationship between uncertainty avoidance and financial reporting.
3. To ascertain the effect of individualism on financial reporting.
4. To examine the influence of masculinity on financial reporting.

1.4 Research questions

The research questions for the study are as follows:

- 1) To what extent does power distance affect financial reporting?
- 2) To what extent does uncertainty avoidance affect financial reporting?
- 3) To what extent does individualism affect financial reporting?
- 4) To what extent does masculinity affect financial reporting?

1.5 Research hypotheses

The formulated research hypotheses for the study are:

- 1) H_0 : There is no significant relationship between power distance and financial reporting.
- 2) H_0 : There is no significant relationship between uncertainty avoidance and financial reporting.
- 3) H_0 : There is no significant relationship between individualism and financial reporting.
- 4) H_0 : There is no significant relationship between masculinity and financial reporting.

1.6 Significance of the study

This study will be of immense importance to accounting bodies, government, accountants, managers of these manufacturing companies and potential/existing shareholders and researchers as it will try to bring to bear, the likely indicators of cultural dimensions. This will as a matter of fact point out the impending dangers of cultural dimensions and its resultant implications on financial reporting.

This study will be of great importance to managers of manufacturing companies as it will suggest ways for proper reporting of financial statements so as to prevent the ugly incidence of non uniformity. Shareholders and potential shareholders of these companies will also benefit from the study as it will highlight the indicators of cultural dimensions thus, guiding the investors in making investment decisions.

2.0 LITERATURE REVIEW AND THEORETICAL FRAMEWORK

2.1 Theoretical framework

There are various theoretical approaches to the structure of values at the cultural level, such as those employed by Hofstede (1984), Triandis (1995) and Schwartz (1994). Hofstede proposes a one dimensional structure called simply *individualism-collectivism*; those cultures that emphasize the autonomy of the person are grouped under individualism, while those cultures who's most important values place emphasis on the dependency of the individual with respect to in-groups are clustered under collectivism. Triandis, Bontempo, Villareal, Asai and Lucca (1988) initially began, like Hofstede, with a unidimensional understanding, but recently (Triandis, 1995; Triandis & Gelfand, 1998) have progressed toward the recognition of bi-dimensionality. Schwartz (1990, 1994), criticizes this dichotomical assignment of values to either individualism or collectivism, and suggests that some values can serve both individual and collective interests. Given that our study focuses only on the comparison of the Hofstede and Schwartz models, we will now proceed to explain each one of them.

Individualism-Collectivism at the Cultural Level: The Hofstede and Schwartz theories

2.1.1 The hofstede theory of cultural dimension

With the publication of *Culture's Consequences*, Hofstede (1984) describes at the cultural level one of the first theoretical orientations towards the structure of values which has individualism as one of their components. This author conducted an important study of values associated with work among employees of a multinational company with branches in more than 40 countries.

The following four factors were sufficient to distinguish among cultures:

1. Power distance: Degree to which members of a society accept as legitimate that power in institutions and organizations are unequally distributed.
2. Avoiding uncertainty: Degree to which members of a society are uncomfortable with uncertainty and ambiguity. This leads them to support beliefs that promise certainty and to maintain institutions that protect conformity.
3. Masculinity/femininity: A preference for accomplishment, heroism, severity and

material success as opposed to a preference for relationships, modesty, attention to the weak and quality of life.

4. Individualism/collectivism: A preference for closed social surroundings in which it is understood that individuals must care for themselves and only their closest relations as opposed to a dependence on groups of which individuals form part.

Individualism, considered as one dimension with two poles, is defined as an assessment of the emotional independence and autonomy of the person. Culture, in this case the mean of a country, is scored high in this factor if there are favorable responses to items such as: «Have a job which leaves you sufficient time for your personal or family life», «Have considerable freedom to adapt your own approach to the job», and «Have challenging work to do – work from which you can get a personal sense of accomplishment.

A country with a high score in collectivism gives more importance to factors such as: Have training opportunities (to improve your skills or learn new skills) and Have good physical working conditions (good ventilation and lighting, adequate work space, etc.).» In other words, they value more what the organization can do for the individual.

According to Hofstede, individualism would reflect the emotional independence of the person with respect to groups and organizations, while its absence would be similar to an emotional dependence and a feeling of us. Individualism is inversely related to the power distance dimension, which is -.64 in Hofstede's original study, and -.70 in the sample of teachers and -.75 in that of students used in Schwartz's cross-cultural study (Schwartz, 1994). Therefore, at least at a cultural level, individualism is the opposite of the acceptance of hierarchy and of ascribed social inequality.

Individualism has been erroneously mistaken with the masculinity-femininity dimension. Hofstede (1998) clarifies that while both dimensions share a relation with a conception of the self, the individualism dimension is related to the individual's position in society while the masculinity-femininity dimension is related to the individual's concept of masculinity or femininity. However, they diverge in a number of aspects. While individualism is connected to the autonomy or dependency of individuals from groups, the masculinity-femininity dimension is related to ego enhancement versus relationship enhancement

regardless of group ties. Moreover, unlike individualism-collectivism, masculinity-femininity is unrelated to wealth.

2.1.2 The schwartz theory of cultural dimension

Schwartz (1990) points out that the individualism-collectivism dichotomy has enjoyed great popularity in cross-cultural psychology, but at the same time it has obscured important differences among some values which are normally associated with it. To this end, he presents three criticisms of why it is not an adequate typology:

- a) There can be values that, because of their nature, serve both personal interests (individualism) and group or collective ones (collectivism). This would be the case of those values that share a motivation for the search for personal, family or national security;
- b) The dichotomy is insufficient because it ignores values that serve collective goals, but are not characteristic of the in-group (i.e. equality for all, social justice, preserving nature, and a world of beauty).

To include these values the theory argues that collectivists show less interest than individualists for strangers (Hui, 1988, Triandis et al., 1988). As observed by Schwartz (1990), if collectivism is defined as a function of the in-group, then one must distinguish between in-group collectivism and universal collectivism; and the dichotomy implies a polar opposition, and there can be individual and collective interests that are not in conflict. For example, hedonism, self-direction or stimulation, are values that serve the interests of the person but not necessarily at the expense of any collectivity. These same values can be placed by leaders or members of a collectivity as goals for all members.

2.2 The concept of national culture

Culture is a very vague concept with manifold definitions (Kroeber and Kluckhohn (1952)). A very common definition was given by the Dutch researcher Geert Hofstede (1984):

Culture is the collective programming of the mind which distinguishes the members of one group or society from those of another. Culture consists of the patterns of thinking that parents transfer to their children, teachers to their students, friends to their friends, leaders to their

followers, and followers to their leaders. Culture is reflected in the meanings people attach to various aspects of life; their way of looking at the world and their role in it; in their values, that is, in what they consider as 'good' and 'evil'; in their collective beliefs, what they consider as 'true' and as 'false'; in their artistic expressions, what they consider as 'beautiful' and as 'ugly'.

As it is illustrated in this definition, values must be established as the most fundamental element of culture. Values are to be understood as the central characteristics of a culture and can be employed to compare different cultures. This basic status of values is reflected in the functional chain of culture from values across attitudes towards behaviour. Value shape attitudes which again form the behaviour of people. This functional chain is empirically verified (Breuer & Quinten, 2008).

2.3 The impact of culture in accounting

From the literature and practice, Gray (1988) identified four accounting value dimensions that can be used to define a country's accounting (sub) culture: professionalism versus statutory control; uniformity versus conformity; conservatism versus optimism, and; secrecy versus transparency. The first two dimensions relate to authority and enforcement of accounting practice at a country level, and the second two relate to the measurement and disclosure of accounting information at a country level. Gray (1988) extends Hofstede's model by overlaying accounting values and systems and their links to societal values and institutional norms. Gray posits that accountants' value systems are related to and derived from the unique societal values in each country.

Essentially, accounting values, in turn, affect accounting systems; therefore cultural factors directly influence the development of accounting and financial reporting systems at a country level (Doupnik & Tsakumis, 2004).

3.0 Research Methodology

3.1 Research Methods

Quantitative research is used for this study. The objective of quantitative research was to develop and employ mathematical models, theories and/or hypotheses pertaining to natural phenomena. The subjects of this study are the financial directors of all the 66 quoted manufacturing companies in the Nigerian Stock Exchange (NSE) market out of which a sample of 57 financial directors were selected. The survey

instrument will be administered to the target samples via mail. The research is conducted by a mail survey instead of online survey. A mail survey is more formal and solemn than an online survey. From there, questionnaires are delivered and collected. The questionnaires are delivered by post and the addressees were the director in the companies selected. The reason is that most of the questions concern with management. A cover letter is attached to the questionnaire in each envelop to introduce the research and describe the purpose of the survey. A prepaid return envelope is attached to the questionnaire sent to respondents to encourage participation and facilitate return of the questionnaire. After getting expert consulting and pilot survey, questionnaires with the same enclose materials were sent to the chosen companies.

3.2 Data Collection

The responded questionnaires were received from the financial directors. Simultaneously, the questionnaires were sent out to 57 financial directors and selected via mail within one month; all of the participants' questions relating to the questionnaire which were clarify via mail address. At the end, 51 participants sent back the answers. Each participant was asked to fill out a questionnaire indicating his or her agreement or disagreement with each statement on a 5-point Likert scale ("1"= Strongly Disagree; "2"= Disagree; "3"= Neutral; "4"= Agree; "5" = Strongly Agree).

3.3 Validity and Reliability

The reliability and validity of the measurement model is necessary to secure its fit to the data. A Cronbach's alpha of 0.7 serves as a cut-off point for assessing reliability for multi-item scales (Cronbach & Meel, 1995; Nunally, 1978). Alpha reliability coefficients will be calculated to check consistency of the scale. Cronbach's alpha coefficients can range from 0.0 to 1.0, and may be interpreted as the percent of

"true score" variance in a multiple item measure. The expert's validity was established by asking for the assistance of three academic research experts to pass judgment on the suitability of the items chosen before conducting the survey. The validity of the survey instrument was identified by taking the square-root of the reliability coefficient as it has been proved that the maximum validity coefficient equals the square-root of the reliability coefficient.

In order to develop questionnaires, after getting expert consultants, a pilot survey of 5 quoted manufacturing was conducted by sending questionnaires to the financial directors of these companies. The pilot survey helps to uncover the real situation of firms and to identify possible irrelevant questions. Based on the pilot survey, the irrelevant questions were eliminated or modified and some new questions were added. In addition, the instrument's reliability was tested by conducting nonparametric- Wilcoxon test in order to identify whether the mean difference is statistically significant or not. This method examines the effect of every demographic factor (non-metric independent variables) on every item (metric dependent variables). Thus, the research applied Cronbach's Alpha coefficient to measure whether the internal consistency of the responses is similar across items and how they represent the variable. The higher the Cronbach's alpha values are, the higher the reliability of the variables data collection.

Using SPSS 19.0 for calculating Cronbach's alpha of the whole items in this research was 0.940 (see table 3-1). This number indicated that the items form a scale that has very good internal consistency or they were regarded as 'high' reliability or that items were measuring the same underlying construct. The Cronbach's Alpha of Power Distance, Uncertainty Avoidance, Individualism and Masculinity as well as firm Financial Reporting are in turn: 0.792, 0.783, 0.721, 0.736 and 0.935 are presented in the table 3-1.

Table 3-1 Cronbach's for all factors

	Factor	Cronbach's Alpha	No. of Items
1	Power Distance	0.792	4
2	Uncertainty Avoidance	0.783	4
3	Individualism	0.721	4
4	Masculinity	0.736	4
5	Financial Reporting	0.935	4
6	Total factor	0.904	20

Source: Researcher's Estimation, 2012

3.4 Regression Analysis

To investigate the relationship between Power Distance, Uncertainty Avoidance, Individualism and Masculinity and Financial Reporting, linear regression analysis is appropriate multivariate technique.

The equation for the linear regression is as follow:

$$Y = b_0 + b_1X_1 + b_2X_2 + b_3X_3 + b_4X_4$$

Where: Y = Financial Reporting

b_0 stands for intercept

$b_1, b_2, b_3,$ and b_4 stand for coefficients

X_1 stands for Power Distance

X_2 stands for Uncertainty Avoidance

X_3 stands for Individualism

X_4 stands for Masculinity

4.0 Results and Interpretation

4.1 Analysis of Variance (ANOVA)

The One-way ANOVA was conducted to answer the research questions. In other words, the analysis aimed to examine whether there was existence of statistically significant difference of

mean on financial reporting across multiple levels of every factor. The test of homogeneity of variances of factors against financial reporting is presented in Table 4-1. It showed that the assumption of homogeneity of variances was met: the Levene's tests were not significant with all p values greater than .05.

Table 4-1: Test of Homogeneity of Variances of Demographic Factors against Financial Reporting

Demographic factors	df1	df2	Levene Statistic	Sig.
Type of company	3	47	2.916	.056
Gender	1	50	.895	.346
Manager's Age	3	47	1.912	.130
Business age	3	47	2.916	.056
Education degree	3	47	2.527	.059

Source: Researcher's Estimation, 2012

Note: * $p < .05$, ** $p < .01$

Table 4-2: presents the analysis result in testing hypothesis concerning the examination of whether there was existence of statistically

significant difference of mean on financial reporting across multiple levels of every demographic factor.

Table 4-2: ANOVA of Demographic Factors against Financial Reporting

Demographic factors	df1	df2	F	Sig.
Type of company	3	47	10.052	.000***
Gender	1	50	2.334	.128
Manager's Age	3	47	6.981	.000***
Business age	3	47	10.052	.000***
Education degree	3	47	118.255	.000***

Source: Researcher's Estimation, 2012

Note: * $p < .05$, ** $p < .01$

The statistics in table 4-2 points out an existence of significant difference in Financial Reporting between the various type of company, $F(3, 47) = 10.052$, $p < .001$, and between the four groups of Manager's Age, $F(3, 47) = 6.981$, $p < .001$. An existence of significant difference in Financial Reporting was also found among groups of demographic factor Business age, $F(3, 47) = 10.052$, $p < .001$. It is also easy to see that there is an existence of significant difference in Financial Reporting between the four groups of Education degree Doctor, Master, Bachelor and under Bachelor, $F(3, 47) = 118.255$, $p < .001$.

4.2 Correlation Analysis

Before applying the regression analysis, the study examines different factors that may affect financial reporting. The analysis was, at first, done by issuing the correlations between pairs of external variables to examine whether there was any existence of relationships between or among those external variables. The result of this correlation analysis is presented in Table 4-3.

The correlation test is firstly conducted to determine the best linear combination of four factors of financial reporting: power distance, uncertainty avoidance, individualism and masculinity. The results of correlation test were presented on the Table 4-3 as below:

Table 4-3: Correlation Coefficients among External Variables under Study

		PD	UA	IND	MAS
	N	51	51	51	51
PD	Pearson Correlation	1			
	Sig. (2-tailed)				
UA	Pearson Correlation	.672***	1		
	Sig. (2-tailed)	.000			
IND	Pearson Correlation	.745***	.733***	1	
	Sig. (2-tailed)	.000	.000		
MAS	Pearson Correlation	.760***	.705***	.736***	1
	Sig. (2-tailed)	.000	.000	.000	

Source: Researcher's Estimation, 2012

Note: PD = Power Distance; UA = Uncertainty Avoidance; IND = Individualism; MAS = Masculinity; * $p < .05$; ** $p < .01$

Table 4-3 shows a highly positive relationship ($r = .672$) between Power Distance (PD) and Uncertainty Avoidance (UA) as well as a positive relationship ($r = .745$) between Power

Distance (PD) and Individualism (IND). Both the relationships between Power Distance and Uncertainty Avoidance, Power Distance and Individualism are significant ($p < .001$).

Concurrently, the strength of positive relationship between Power Distance and Masculinity (MAS); are regarded strong ($r = .745$, $r = .760$, respectively). All these two relationships are significant ($p < .001$). Similarly, a highly positive

relationship between Uncertainty Avoidance and Individualism, Uncertainty Avoidance and Masculinity, also are indicated in the table 4-3 ($r = .733$, $r = .705$, respectively).

4.3 Variables Predicting Financial Reporting

Table 4-4: Regression Analysis for Variables Predicting Profitability for total sampling

Model Variables)	(Independent	Unstandardized Coefficients		Standardized Coefficients	<i>t</i>	Sig.
1		<i>B</i>	<i>Std. Error</i>	<i>Beta</i>		
	(Constant)	-3.176	.258		-12.323	.000***
H ₁	Power Distance	.218	.120	.121	2.146	.000***
H ₂	Uncertainty Avoidance	.303	.099	.174	3.044	.000***
H ₃	Individualism	.354	.112	.194	3.164	.000***
H ₄	Masculinity	.190	.100	.110	1.901	.059

Equation 1

$$FR = -3.167 + .121PD + .174UA + .194IND + .110MAS$$

<i>R</i>	.910
<i>R</i> ²	.828
<i>Adjusted R</i> ²	.822
<i>F</i> (4, 46)	157.571***

Source: Researcher's Estimation, 2012

Note: PD = Power Distance; UA = Uncertainty Avoidance; IND = Individualism; MAS = Masculinity; * $p < .05$; ** $p < .01$

Table 4-4 indicates that the model was significant with $F(4, 46) = 157.571$, $p < .001$ which showed that the four above predictor variables constituted a fairly good model and significantly predicted Financial Reporting. The Adjusted R^2 value was .822 indicated that about 82% of the variance in Financial Reporting was explained by the model. Model reveals that the three independent variables Power Distance, Uncertainty Avoidance and Individualism contributed significantly to the predicting of Financial Rep[orting] ($t = 2.146$, $p < .001$; $t =$

3.044 , $p < .001$; $t = 3.146$, $p < 0.001$; respectively).

From the Table 4-4 the formula can be written as following:
Financial Reporting (FR) = $-3.176 + 0.121 \times$
Power Distance + $0.174 \times$ Uncertainty Avoidance
+ $0.194 \times$ Individualism + $0.110 \times$ Masculinity.

In conclusion, the results of the regression confirm that three factors Power Distance, Uncertainty Avoidance and Individualism, have a positive impact on Financial Reporting. However, Masculinity does not have a positive impact on Financial Reporting.

Hypothesis	Content	Expected change	Results
H ₁	Power Distance has positive impact on Financial Reporting	Increase	Supported
H ₂	Uncertainty Avoidance has positive impact on Financial Reporting	Increase	Supported
H ₃	Individualism has positive impact on Financial Reporting	Increase	Supported
H ₄	Masculinity has positive impact on Financial Reporting	X	Not supported

Source: Researcher's Estimation, 2012

5.0 RECOMMENDATIONS

Based on the findings of the study, it is recommended that cultural dimensions serve as a basis for a number of risks of material misstatements in the financial reporting process. Therefore culture should be directly linked to financial reporting as it is potentially useful for users of accounting information because this provides them with supplementary information on the likelihood of material errors in financial statements. Finally, there should be harmonization of financial reporting rules Nation wide by adopting the International Financial Reporting Standards (IFRS).

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