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An analysis of social factors influencing the adoption of International Financial Reporting Standards

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Abstract: This paper examines the decision of 120 countries to permit or not to permit the use of International Financial Reporting Standards (IFRS) for listed companies incorporated within their borders. An empirical model is developed considering variables related to culture, political systems and economic systems of the countries. Least squares regression was used to examine which variables significantly influence the decision to allow the use of IFRS. The results from this regression indicate that literacy rates and net import activity positively influence the decision to allow IFRS. Less economically developed countries were also shown to be more likely to allow IFRS. A model using these three variables was used to predict whether countries would allow IFRS. The model was able to statistically improve on the prediction that all countries would use IFRS.

Keywords: international accounting; adoption of IFRS; social factors; culture; political systems; economic systems; prediction of IFRS use; net imports; resource dependence; economic development; literacy; International Financial Reporting Standards; IFRS.

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1 Introduction

The 'society of states' model views international law as an ordered social space in which states are the members (Garcia, 2005; Beitz, 1979). States are considered to be autonomous and generally practice self-determination. Accounting systems were developed by each state within such principles. Most nations established their own system to satisfy their own needs. These accounting systems vary widely. Nair and Frank (1980), for example, classify these systems as the British Commonwealth model, the Latin American model, the Continental European model and the US model.

Rawls (1971) describes five 'circumstances of justice': moderate scarcity of resources, shared geographic territory, a capacity to help or harm one another and that people are both non-altruistic and hold conflicting claims. Globalisation is creating these circumstances at an international level (Garcia, 2005). International trade and financial markets are allocating resources on a global scale. Technology is eliminating space and time as factors in social interaction and creating a global community. Globalisation is creating the need for global public law as well as local and national public law.

International Financial Reporting Standards (IFRS) help fulfil the need for global public law in the financial resources arena by regulating financial reporting at the global level. Companies need to be able to raise capital on a global basis. Investors need to be able to invest anywhere in order to optimise returns versus risk. Lack of similar accounting standards has been cited as a major reason for the inability of investors to optimise their investment portfolios (Choi and Levich, 1991).

A variety of policies with respect to the use of IFRS have evolved at the national level. Some countries require the use of IFRS for domestic listed companies. Other countries require their use for certain types of companies like banks. Still other countries permit companies to use IFRS if they so choose and domestic standards if they do not. Many countries still do not permit IFRS at all. A number of countries, particularly in the European Union, have recently adopted IFRS for domestic listed companies. This study relies on IAS Plus (Deloitte, 2004) to classify countries into categories of use of IFRS. IAS Plus (Deloitte, 2004) categorises countries into four levels of IFRS usage: IFRS not permitted, IFRS permitted, required for some domestic listed companies and required for all domestic listed companies. To be considered permitting in these categories, the direct use of IFRS is required. Documentation of direct use would include listing IFRS as the basis of accounting in company accounting policy notes and/or the auditor's report referring to the use of IFRS.

Why have these different policies been adopted? What local customs and needs influence this decision? Before the current adopters, IFRS were primarily adopted by countries with developing economies. Not all developing economies, however, have adopted IFRS and a number of developed countries allow or require the use of IFRS. Therefore, factors other than development are important in explaining the country-level decision on use of IFRS versus local generally accepted accounting principles (GAAP). Because this is a country-level decision (except for the European Union), the influential factors relate to societal norms and values and economic indicators that differ among countries. Policy makers and other interested parties need to understand these influences as countries with developing economies continue to consider the option of adopting IFRS.

The purpose of this study is to empirically identify these factors that influence the adoption of IFRS. The factors considered are social structures, including cultural variables, political systems and economic structures. These factors have been shown to influence international accounting in prior literature papers (Nair and Frank, 1980; Goodrich, 1986; Douplik and Salter, 1995; Dumontier and Raffournier, 1998; Salter, 1998; Archambault and Archambault, 2003) but have not been previously studied jointly in the IFRS decision. The analysis will concentrate on those countries allowing use of IFRS before 2005. Many of the more recent adoptions of IFRS have been for political reasons (Stoddart, 2000). Including these adopters would reduce the ability of the model to detect the forces that drove the initial adopters to IFRS usage and reduce the ability of the results to be useful to policy makers in making decisions about adopting IFRS by countries with developing economies.

Results indicate that countries are more likely to permit IFRS as literacy and import activity increase. Developed nations are less likely to permit IFRS than developing and undeveloped countries. When the model was used in a discriminant analysis to determine which countries would be expected to use IFRS, several members of the European Union were classified as not permitting IFRS even though the countries were already permitting the use of IFRS in 2004. This indicates that the European Union adopted IFRS for different reasons than countries with developing economies.

Political systems as measured by political rights, civil liberties and legal system (code law versus common law) are not found to influence the adoption of IFRS. The inflation rate and foreign stock exchange listings are also shown to not be significant. Countries receiving higher levels of foreign aid were found, contrary to expectations, to be less likely to permit IFRS. Foreign aid, however, was not significant in the stepwise regression.

The next section of the paper reviews the existing literature and develops hypotheses. This is followed by a discussion of data and methodology. Results are then discussed. Conclusions are discussed in the final section.

2 Theory development

Accounting is a social system that exists within the context of larger social systems. These sets of social systems are what make each country unique. Accounting systems respond to changes in other social systems. Because accounting is one of the social systems, society changes in response to changes in accounting systems as well (Harrison and McKinnon, 1986). Archambault and Archambault (2003) model corporate disclosure as a function of culture, national political and economic systems and corporate financial and operating systems. They find that all of these systems influence the corporate disclosure decision.

This paper uses a similar approach in the study of the adoption of IFRS at the national level. In particular, this study seeks to determine whether national culture, political systems and economic systems influence the national policy regarding the use of IFRS. Corporate systems are not considered because this paper is limited to national accounting standard choice not the choice of particular companies in countries where IFRS is permitted but not required.

2.1 Culture

This study utilises the level of education as an important cultural element (Doupnik and Salter, 1995)¹. Countries with high literacy rates are expected to have a more global perspective and the ability to read and understand IFRS. Therefore, these countries are more likely to permit the use of IFRS.

H1 Countries with high literacy rates are more likely to permit the use of IFRS.

2.2 Political systems

Political freedom can be measured in terms of political rights and civil liberties. Political rights represent the ability to participate in the political process through such means as voting. Civil liberties represent individual freedom from state control (McColm, 1992). The ability of companies to engage in international trade and to choose relevant accounting policies should increase with political freedom (Goodrich, 1986; Deese, 1998; Salter, 1998). Therefore, countries with political freedom should be more likely to permit the use of IFRS.

H2 Countries with a high level of political freedom are more likely to permit the use of IFRS.

Legal system may also influence the use of IFRS. Common law countries are characterised by case law, judicial solutions to individual cases. Countries with the Romano-Germanic legal system are characterised by codified laws, often including national accounting standards. Salter and Doupnik (1992) demonstrate that the legal system is related to accounting practices². Common law systems may be more able to evolve accounting systems to satisfy specific needs (Ball et al., 2000). As a result, countries with common law systems may be more likely to permit the use of IFRS.

H3 Countries with common law legal systems are more likely to permit the use of IFRS.

2.3 Economic systems

The accounting profession emerged during the late 18th and early 19th centuries during the same time that the developed economies were modernising. As a result, countries with developed economies tend to have a well organised accounting profession with an established accounting standard development process. This existing, highly organised profession and accounting system is consistent with the 'society of states' model (Garcia, 2005). Countries with developing economies may not have an established accounting profession and may be more likely to permit the use of IFRS as an approach to quickly modernising their financial reporting system (Joshi and Ramadhan, 2002).

H4 Countries with developing economies are more likely to permit the use of IFRS.

Archambault and Archambault (1998) report that countries with high inflation rates are more likely to adopt inflation accounting. IFRS provide guidance on accounting for inflation. Improved comparability with financial reporting in other countries may be of more value in an inflationary environment. Countries with high inflation, furthermore, tend to have developing economies and may not have a well developed accounting

profession to deal with these reporting issues. As a result, countries with high inflation may be more likely to permit the use of IFRS.

H5 Countries with high inflation rates are more likely to permit the use of IFRS.

Firms compete in the international financial markets to raise capital. Firms that list on foreign exchanges may have an incentive to report using IFRS (Dumontier and Raffournier, 1998). Also, the use of IFRS may be acceptable on both the domestic and foreign exchange, reducing reporting costs over producing a report in the domestic GAAP of the issuer and then a form of GAAP acceptable on the foreign exchange. As a result, countries that have firms listed on foreign exchanges may be more likely to permit the use of IFRS.

H6 Countries with firms that list on foreign stock exchanges are more likely to permit the use of IFRS.

Firms also compete in product markets. Zarzeski (1996) describes this as international resource dependence. Murphy (2000) cites the need for IFRS to expand international trade. Countries that import a significant amount of goods will contain companies that buy these goods on credit. IFRS may help these companies to obtain credit or credit on more favourable terms because the statements can be more easily understood than if domestic standards were used. As a result, countries that import a significant amount of goods may be more likely to permit the use of IFRS to facilitate international trade.

H7 Countries with high levels of imported goods are more likely to permit the use of IFRS.

Many countries receive foreign aid to help develop their economy. The World Bank, for example, engages in numerous programs to improve infrastructure, education and financial markets in countries with developing economies. Coordinating agencies such as the World Bank, bring economic, social and symbolic capital (Neu et al., 2002) to the development process. They introduce best practices to help implement the programs. Countries dependent upon foreign aid may have incentives to adopt IFRS (Mir and Rahaman, 2005) as a condition for receiving that aid. As a result, countries that receive foreign aid may be more likely to permit IFRS.

H8 Countries with high levels of foreign aid are more likely to permit the use of IFRS.

3 Data and methodology

IAS Plus (Deloitte, 2004) classifies countries as not permitting IFRS, permitting IFRS for domestic listed companies, requiring IFRS for some domestic listed companies or requiring IFRS for all domestic listed companies. This data set includes 133 countries from throughout the world and includes all countries for which Deloitte has information. IAS Plus, therefore, is used to determine which countries permit or require the use of IFRS for some or all domestic listed companies. IAS Plus only considers direct use of IFRS, in which the basis of accounting note and auditor's report refer to IFRS. Any level of permitted use is considered to be an adopting country for this study because the country, by allowing some use of IFRS, is accepting IFRS as a set of standards that meet the financial reporting needs of companies within the country's borders.

For each country in the sample, the amount of imports and exports and the inflation rate (all for 2004) were gathered from the *World of Information* internet site. The literacy rate, legal system (common law or code law) and foreign aid were gathered from the *World Factbook*. Developed economies were identified from the World Bank classification as disclosed in its *Millennium Development Goals*.

Political freedom was measured by the political rights and civil liberties scores reported by Freedom House. Political rights represent the ability to participate in the political process through voting and other means. Civil liberties represent individual freedom (McColm, 1992). Political rights and civil liberties are scaled from one to seven, with one representing high political freedom.

The foreign listing variable was developed by collecting the foreign companies listed on the six stock exchanges with major foreign listings according to the World Federation of Exchanges. The stock exchanges considered were the London, New York, Nasdaq, Euronext, Luxembourg and Swiss. The listings for each exchange were obtained and the country of origin for each foreign listing was determined. The variable was coded as one if a country had at least one company listed on any of these exchanges.

Some countries included in IAS Plus could not be included in the analysis because of missing data. Literacy rates were not available for five countries. Political rights and civil liberty scores were not included in Freedom House for an additional five countries. One more country was not clearly classified in the *World Factbook* as having either a code or common law legal system. Missing import and export data and foreign aid information caused the loss of two additional countries. These missing data points reduced the data set to 120 countries.

The hypotheses are tested using the following regression model:

$$IS = a + b_1LT + b_2PR + b_3CL + b_4LG + b_5DV + b_6IF + b_7FOR + b_8IE + b_9FAID + e$$

where:

IS = 1 if country permits or requires IFRS for some or all domestic companies prior to 2005, 0 otherwise

LT = literacy rate

PR = political rights score

CL = civil liberties score

LG = 1 if the country uses a common law legal system, 0 if code law legal system

DV = 1 if the country is developed, 0 otherwise

IF = inflation rate

FOR = 1 if developing country has at least one company listed on a major foreign exchange, 0 otherwise

IE = ratio of imports to exports

FAID = foreign aid as a percentage of gross domestic product.

The F-statistic is used to test the overall explanatory power of the model. Individual hypotheses are tested with the t-statistic.

4 Results

Table 1 provides the classification by IAS Plus (Deloitte, 2004) at the end of 2004 for each of the 120 countries in the data set. Table 2 shows the descriptive statistics for these countries. 58% of the countries considered permit IFRS usage. Common law is used by 32% of the countries considered. Only 20% of the countries analysed are considered to be developed by standards established by the World Bank. At least one company in 35% of the developing countries considered trades on a foreign exchange. More countries are net importers than net exporters as shown by the median input to export ratio being over one. Table 1 also shows that for the continuously measured variables (literacy, inflation, imports/exports and foreign aid) the sample has high variability as noted by the standard deviation of these variables.

Table 3 summarises the results. The purpose of this study is to determine those national-level factors that significantly explain a country's choice to permit or not permit the use of IFRS³. This study examines the choice prior to 2005 to avoid possible effects of the political process of the European Union (EU) adoption of IFRS and to concentrate on decisions made by individual countries. Model A presents the complete set of variables considered and is significant at the 2% level. Countries are more likely to permit the use of IFRS as import activity and literacy increase. As expected, developed nations are less likely to permit IFRS. The results for literacy support H1, that cultural factors significantly influence the choice to permit the use of IFRS. The development result is consistent with H4 and the import/export result is consistent with H7, both indicating that economic conditions of a country are significant factors in the choice of accounting policy.

Table 1 AIS Plus listings for the data set

<i>IFRS not permitted</i>	<i>IFRS permitted</i>	<i>IFRS required for some domestic listed companies</i>	<i>IFRS required for all domestic listed companies</i>
Argentina#	Belgium@	Bahrain	Armenia
Australia	Bolivia	Brunei Darussalam	Austria@
Benin	Botswana@	China	Bahamas
Bhutan	Denmark@	Czech Republic	Barbados
Brazil#	Dominica	Hungary	Bangladesh@
Burkina Faso	El Salvador	Kazakhstan	Bulgaria
Cambodia	Estonia	Romania	Costa Rica
Canada	Finland@	Russian Federation	Croatia
Chile#	Germany@	Ukraine	Cyprus
Cote D'Ivoire	Hong Kong	United Arab Emirates	Dominican Republic
Columbia#	Laos@		Ecuador
Fiji#	Latvia		Egypt
France	Lesotho		Georgia
Ghana#	Lithuania		Guatemala
Greece	Luxembourg@		Guyana

Notes: # Classified to permit but does not permit.

@ Classified as not permit but permit.

Table 1 AIS Plus listings for the data set (continued)

<i>IFRS not permitted</i>	<i>IFRS permitted</i>	<i>IFRS required for some domestic listed companies</i>	<i>IFRS Required for All domestic listed companies</i>
Iceland	Namibia		Haiti
India	Netherlands@		Honduras
Indonesia#	South Africa		Jamaica
Ireland	Swaziland		Jordan
Israel#	Switzerland@		Kenya
Italy	Turkey		Kuwait
Japan	Uganda		Kyrgyzstan
Korea (South)	Zambia		Lebanon
Mali	Zimbabwe		Malawi@
Malaysia#			Malta
Mexico#			Mauritius
Moldova#			Nepal@
Mozambique			Nicaragua
New Zealand			Oman
Niger			Panama
Norway			Papua New Guinea@
Pakistan			Peru
Philippines#			Tajikistan
Poland#			Tanzania
Portugal			Trinidad and Tobago
Saudi Arabia#			
Singapore#			
Slovenia#			
Spain			
Sri Lanka#			
Sweden			
Syria#			
Thailand#			
Togo#			
Tunisia#			
UK			
USA			
Uruguay#			
Uzbekistan#			
Venezuela#			
Vietnam#			

Notes: # Classified to permit but does not permit.

@ Classified as not permit but permit.

Table 2 Descriptive statistics (for data set of 120 countries)

<i>Variable</i>	<i>Mean</i>	<i>Median</i>	<i>Standard deviation</i>
IS	0.575	1.000	0.496
LT	84.817	93.000	18.539
PR	3.008	2.000	2.031
CL	3.075	3.000	1.671
LG	0.317	0.000	0.467
DV	0.200	0.000	0.402
IF	6.882	3.650	10.861
FOR	0.350	0.000	0.479
IE	1.420	1.152	1.043
FAID	1.090	0.277	1.943

Notes: IS = 1 if country permits or requires IFRS for some or all domestic companies prior to 2005, 0 otherwise
 LT = literacy rate
 PR = political rights score
 CL = civil liberties score
 LG = 1 if the country uses a common law legal system, 0 if code law legal system
 DV = 1 if the country is developed, 0 otherwise
 IF = inflation rate
 FOR = 1 if developing country has at least one company listed on a major foreign exchange, 0 otherwise
 IE = ratio of imports to exports
 FAID = foreign aid as a percentage of gross domestic product.

The variables representing political rights, civil liberties and legal system are not significant. Thus H2 and H3 are not supported. The political system does not seem to affect the decision to permit the use of IFRS.

The variables representing inflation and foreign listings are also not significant. The coefficient on foreign aid is marginally significant but opposite the expected sign. Higher levels of inflation, the existence of companies listing on foreign exchanges and reliance on foreign aid do not seem to be significant factors in the national decision to permit the use of IFRS. Thus, H5, H6 and H8 are not supported.

To focus on significant variables, the model was also estimated using stepwise regression. The results are presented in Model B of Table 3. Development, literacy and import/export activity are all shown to be significantly related to the choice to permit IFRS. The stepwise model did not select any other variables as adding significant explanatory power to the national-level decision to permit the uses of IFRS.

To further test the classification ability of the model, the results of the stepwise regression were used to estimate the probability of permitting IFRS use for all 120 countries considered in the model estimation. Using a cut-off value of 0.5 and higher for the dependent variable as being a country that would permit the use of IFRS, the model estimated that 66.7% of the 120 countries would permit IFRS use. This is a larger group than actually do permit use of IFRS. The model correctly classified 67.5% of the countries. This rate of correct classification is significantly better than the 57.5% correct classification that would occur if the naive model of classifying all countries as permitting the use of IFRS were used to make the classification (t-statistic 2.12,

p-value < .01). The model, therefore, has classification ability providing additional support for its validity as a model explaining the national-level choice to permit the use of IFRS.

Table 3 Regression models

Variable	Model A		Model B	
	Coefficient	t-statistic	Coefficient	t-statistic
Constant	0.1392	0.42	-0.0469	0.45
LT	0.0057	1.97 **	0.0067	2.68 ***
PR	0.0470	0.73		
CL	-0.0779	-0.89		
LG	0.0007	0.99		
DV	-0.4164	-2.80 ***	-0.3800	-3.25 ***
IF	0.0054	1.26		
FOR	-0.0445	-0.44		
IE	0.1142	2.33 ***	0.0910	2.17 **
FAID	-0.0349	-1.31 *		
Model:		p-value		p-value
Adjusted R ²	9.7%		13.84%	
F-statistic	2.43	0.015 **		
Sample	120		120	

Notes: *10% significance

**5% significance

***1% significance.

$$IS = a + b_1LT + b_2PR + b_3CL + b_4LG + b_5DV + b_6IF + b_7FOR + b_8IE + b_9FAID + e$$

where:

IS = 1 if country permits or requires IFRS for some or all domestic companies prior to 2005, 0 otherwise

LT = literacy rate

PR = political rights score

CL = civil liberties score

LG = 1 if the country uses a common law legal system, 0 if code law legal system

DV = 1 if the country is developed, 0 otherwise

IF = inflation rate

FOR = 1 if developing country has at least one company listed on a major foreign exchange, 0 otherwise

IE = ratio of imports to exports

FAID = foreign aid as a percentage of gross domestic product.

Symbols by the countries in Table 1 indicate the 39 countries that were not properly classified by the model. Of the incorrectly classified countries, 25 are countries that the model predicts would permit the use of IFRS but do not permit their use (labelled with a #). The other 14 countries currently permit the use of IFRS while the model predicted that they would not use IFRS (labelled with an @). The existence of 25 countries that exhibit the characteristics of countries that would permit the use of IFRS demonstrates the potential for continued growth in the use of IFRS. All of these nations are developing countries.

Table 4 provides contingency tables that examine in more detail the predictive ability of the model. The classification ability of the model varied by region and level of economic development. The model predicted that all 15 members of the EU with developed economies would not permit IFRS. Given that seven of the 15 members did permit IFRS prior to 2005, the model only classified 53.3% of these countries properly.

Table 4 Contingency tables for model prediction

<i>Entire data set</i>			
<i>Predicted</i>			
<i>Actual</i>	<i>Permit</i>	<i>Not permit</i>	<i>Total</i>
Permit	55	14	69
Not permit	25	26	51
Total	80	40	120
<i>EU developed countries</i>			
<i>Predicted</i>			
<i>Actual</i>	<i>Permit</i>	<i>Not permit</i>	<i>Total</i>
Permit	0	7	7
Not permit	0	8	8
Total	0	15	15
<i>EU developing countries</i>			
<i>Predicted</i>			
<i>Actual</i>	<i>Permit</i>	<i>Not permit</i>	<i>Total</i>
Permit	9	0	9
Not permit	2	0	2
Total	11	0	11
<i>Non-EU developed countries</i>			
<i>Predicted</i>			
<i>Actual</i>	<i>Permit</i>	<i>Not permit</i>	<i>Total</i>
Permit	0	1	1
Not permit	0	8	8
Total	0	9	9
<i>Non-EU developing countries</i>			
<i>Predicted</i>			
<i>Actual</i>	<i>Permit</i>	<i>Not permit</i>	<i>Total</i>
Permit	46	6	52
Not permit	23	10	33
Total	69	16	85

Among members of the EU with developing economies, the model classified all 11 members as permitting IFRS. In fact, nine of these 11 countries did permit IFRS prior to 2005. The model properly classified 81.8% of these countries. This is greater than the 57.5% that would be properly classified using the naive model (t-statistic 1.33, p-value

0.107), though it is not a significant improvement in classification ability at conventional levels.

For the developed economies that are not members of the EU, the model properly classified eight of the nine countries as not permitting IFRS. This result shows marginally improved predictive ability of the model over simply assuming all countries are IFRS users (t-statistic 1.57, p-value 0.078).

The model properly classified 56 of the 85 nations with developing economies that are not members of the EU. For the 56 properly classified countries, IFRS was permitted by 46 countries and not permitted by ten countries. The model classified six countries as not permitting IFRS that in fact do permit IFRS and 23 countries as permitting IFRS that do not permit IFRS. A chi-square test was used to evaluate the classification ability of these countries. The result indicates that the model does significantly aid classification (chi-square 4.66, p-value 0.03).

The results from the model prediction indicate that several countries with developing economies may permit IFRS in the future. Examining members of the EU, the model does not explain the adoption of IFRS by members with developed economies.

Overall the high-level of correct classification of Model B indicates that the model does include those variables that explain most countries' choices between permitting IFRS and only permitting domestic GAAP. The adjusted R^2 of 13.84% and the 39 improperly classified countries indicate that additional variables exist that explain this choice, but this model does help to explain a number of factors that are important in this choice.

The study has focused on pre-2005 IFRS choice because those were countries that made the choice before the EU required the adoption of IFRS. The motivation of the pre-2005 adopters was other than politically motivated. As the Model B predictions show, the model developed in this paper does not work as well at classifying EU countries (the model did not perform better than assuming all EU countries permit IFRS use) as countries from the rest of the world (where the model performed significantly better at predicting use or non-use than assuming all countries permit IFRS use). There has been a significant increase in the number of countries permitting the use of IFRS since 2004. The same variables were used in a regression using AIS Plus country classification in 2006. The results of this regression are shown in Table 5. These results show model misspecification since the regression is not significant at the 5% level. The literacy and import/export variables remained significant, but the most significant variable in the previous model development, lost significance. Development is no longer a motivating force in the national choice of permitting the use of IFRS. This is yet more evidence that more recent adopters are motivated by different issues than the original adopters of IFRS (Stoddart, 2000). Additional research needs to be conducted to understand the variables that are motivating adopters of IFRS since 2004. Also, future researchers in this area should consider dichotomising the sample of IFRS adopters based on time period of adoption since the motivational factors leading to the country choosing to permit the use of IFRS differ over time.

Table 5 Regression model using 2006 IAS Plus country data

<i>Variable</i>	<i>Coefficient</i>	<i>t-statistic</i>
Constant	0.2596	0.85
LT	0.0054	2.04 **
PR	0.0249	0.42
CL	-0.0595	-0.75
LG	0.0444	0.50
DV	-0.0011	-0.01
IF	0.0060	1.54 *
FOR	-0.0517	-0.57
IE	0.0974	2.19 **
FAID	-0.0345	-1.44
Model		p-value
Adjusted R ²	6.1%	
F-statistic	1.84	0.069
Sample	117	

Notes: *10% significance

**5% significance

***1% significance.

$$IS = a + b_1LT + b_2PR + b_3CL + b_4LG + b_5DV + b_6IF + b_7FOR + b_8IE + b_9FAID + e$$

where:

IS = 1 if country permits or requires IFRS for some or all domestic companies prior to 2006, 0 otherwise

LT = literacy rate

PR = political rights score

CL = civil liberties score

LG = 1 if the country uses a common law legal system, 0 if code law legal system

DV = 1 if the country is developed, 0 otherwise

IF = inflation rate

FOR = 1 if developing country has at least one company listed on a major foreign exchange, 0 otherwise

IE = ratio of imports to exports

FAID = foreign aid as a percentage of gross domestic product.

5 Conclusions

This study reports that the choice to permit the use of IFRS, prior to 2005, at the national-level is influenced by import activity, literacy rates and economic development.

The influence of economic development is not surprising, as early adopters of IFRS were nations with developing economies. Adoption of IFRS quickly modernised financial reporting systems and eased access to international capital for these countries. Increased globalisation, however, has spread the acceptance of these standards to other countries as well.

Adoption of IFRS is more likely as literacy increases. This finding supports the assertion that literacy improves the ability of people to engage in international trade and create a global community (Garcia, 2005).

Competition for global scarce resources is expected to create a need for global regulation of reporting (Rawls, 1971). Import activity, a measure of international resource dependency (Zarzeski, 1996), is shown to increase the probability of permitting the use of IFRS.

Much attention has been focused on IFRS being necessary to improve access to international capital via exchanges. The coefficient on the variable representing foreign listings, however, is not significant. As a result, international resource dependency was found to be a more significant influence on the adoption of IFRS at the national level than are international financial markets. However, foreign listing is a choice by firms rather than nations. The foreign listing variable may be a more significant variable when considering a company's choice between IFRS and domestic GAAP within those countries that allow either to be used. This study focused on national-level choices for standards and the results showed the importance of national culture and economic factors in influencing that choice. Future research can focus on the choice of IFRS and domestic GAAP choice at the company level.

The results also showed that more recent IFRS adopters in the EU, Australia and New Zealand do not fit the model for adopters that were generated using 2004 data. To understand these more recent choices, additional research needs to be conducted. Even the model presented in this paper, while significantly explaining pre-2005 IFRS permission choices, had low explanatory power when considering more recent adopters. Additional research is needed to more fully understand the choices made by all countries choosing to adopt IFRS and those choosing not to adopt. If the goal of all countries in the world using IFRS is to ever be met, policy makers at the International Accounting Standards Board need a better understanding of what factors are preventing acceptance.

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