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Global Auditing and Accounting Confusion

If a company is all over the world, which auditing and accounting standards does it use?

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EXECUTIVE SUMMARY

- WHEN POSTING THEIR financial statements on the Internet, multinational companies do not always clarify under which countrys GAAS/GAAP the statements were audited or prepared.

- INCREASED GLOBALIZATION and Internet use makes clear GAAS and GAAP labeling essential.

- WITHOUT CLOSE STUDY, its hard to tell which is the true home country of a given corporation; financial statement users cannot make assumptions.

- SAS no. 58, *Reports on Audited Financial Statements* , needs to be updated to reflect the international nature of business today.

- U.S. GAAS AND GAAP are clear and rigorous. As a matter of pride for the U.S. CPA profession, statements prepared and audited under U.S. standards should be so marked.

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The standard audit report, which was expanded a scant decade ago (see Statement on Auditing Standards no. 58, *Reports on Audited Financial Statements*), should be amended again to say—to an international investing community—that it specifically refers to U.S. standards.

Initially, we had thought of this as a desirable—but not essential—change because of the diversity of generally accepted auditing standards and generally accepted accounting principles from country to country. Now, however, we believe the Internets easy ability to break down restrictions on the distribution of financial statements makes this change an absolute necessity. Expansion of the auditors report is a logical extension of the guidance provided by Statement on Auditing Standards no. 51, *Reporting on Financial Statements Prepared for Use in Other Countries* (AU 534) and is consistent with the guidance provided by the International Standards on Auditing (AU 8700.22).

AUDITING AND ACCOUNTING DIVERSITY

Auditing and accounting standards vary from country to country largely because of differing business practices, fiscal systems and company law. Worldwide uniformity of auditing and accounting standards is an objective of the International Federation of Accountants (IFAC) and the International Accounting Standards Committee (IASC). A number of developing countries have adopted the international standards set by these bodies as benchmarks for their national standards; however, developed countries are moving more cautiously from their own well-established standards to international standards. Thus, auditing and accounting diversity will continue to be a fact of life.

An Internet search turned up 92 stock exchanges all over the world:

Africa	3
Asia	22
Europe	32
Middle East	5
North America	16
South America	14

WHO IS US?

Despite this diversity, it used to be easy for a user of financial statements to identify the national origin of companies and the basis of presentation of their financial statements. U.S. companies used U.S. GAAS and GAAP and French companies used French GAAS and GAAP. However, such easy identification of the "home" country of multinational enterprises is becoming a thing of the past. Former Secretary of Labor Robert Reich suggested in a January 1990 *Harvard Business Review* article (aptly titled "Who Is Us") that, as our economy continues to become truly global, it will become increasingly difficult to identify an entity as "American." Is a company a U.S. company if it

- Is incorporated in Delaware?
- Has shareholders all over the world?
- Has manufacturing operations and most of its employees in Asia?
- Sells most of its products in member countries of the European Union?

THE INFORMATION AGE

Although U.S. auditors and accountants might agree to expand the audit report language for U.S. company financial statements that are distributed worldwide, they probably would consider it irrelevant for statements that will likely remain in the United States. Such a distinction might have made sense a year or two ago, but the Internet has changed all that. Companies of all sizes have home pages on the World Wide Web that offer information requiring only a "point and click" for access (see "When the Bottom Line Is Online," (/issues/1997/mar/botmline.html) JofA, Mar.97). Annual and quarterly reports often are part of this menu of offerings, and their readers could be sitting almost anywhere in the world. Thus, limited distribution is no longer a safe assumption.

The exhibit below, conveys both the reality and the extent of the need for standards identification. The 10 companies listed, which have easily accessed Web sites, sell products or services familiar to consumers in the United States and around the world. Many of us would characterize companies 1 and 2 as Japanese, yet their financial statements are described as being in accordance with U.S. standards. Companies 3 and 4 presumably are German; however, since they have not provided audit reports, there is no indication of the source of the standards. Company 5 is headquartered in Finland, but its financial statements are described as being in accordance with international standards. And, finally (and not surprisingly), the audit reports of the presumably U.S. companies (6-10), do not indicate the source of the standards.

Financial Reporting on the Internet

Company	Internet Address (http://www.)	Source of Standards
1. NEC	nec.com (http://www.nec.com/)	United States [1]
2. Sony	sony.com (http://www.sony.com/)	United States [1]
3. Bayer	bayer.com (http://www.bayer.com/)	Germany [2]
4. Daimler-Benz	daimlerbenz.com	Germany [2]
5. Nokia	nokia.com (http://www.nokia.com/)	International [3]
6. Digital	digital.com (http://www.digital.com/)	United States [4]
7. EDS	eds.com (http://www.eds.com/)	United States [4]
8. MCI	mci.com (http://www.mci.com/)	United States [4]
9. Motorola	motorola.com (http://www.motorola.com/)	United States [4]
10. Netscape	netscape.com (http://www.netscape.com/)	United States [4]

[1] The audit report was signed by a Big Six firm with a Tokyo letterhead. U.S. GAAP is specified as the source of the accounting principles; however, the source of the GAAS is not indicated.
[2] The audit report was not provided by the company; however, other factors imply the use of German standards.
[3] The audit report was not provided by the company; however, the financial statements are described as international accounting standards financials.
[4] The U.S. standard audit report was used and signed by auditors in the United States; therefore, it is assumed that U.S. GAAS and GAAP were involved.

Note : Web site descriptions were accurate when the article was written, but sites are subject to frequent changes.

AN AUDIT REPORT FOR THE INFORMATION AGE

From the late 1940s through the late 1980s, the standard audit report did not change. In 1988, SAS no. 58 established a three-paragraph format, added additional content and changed some of the standard language. SAS no. 58 was one of nine expectation gap auditing standards intended to improve communications between auditors and the readers of financial statements.

If the auditors report identified the source of GAAS and GAAP, financial statement readers would be better able to judge the reliability and relevance of financial information. Companies could make this information available in printed copies and on the Internet at little cost.

PRIDE

Expanding—that is, clearly labeling—the auditors report is important to users of financial statements so they can effectively judge the assurance level of an entitys financial statements. We also see another reason to champion specification, particularly regarding U.S. GAAS and U.S. GAAP. U.S. standards are arguably the best in the world. Subtle endorsement of this opinion is provided by the results of a recent survey (see "Raising Capital Overseas," (/issues/1997/feb/raising.html) JofA, Feb.97), which showed that U.S. GAAP financial statements are accepted by many stock exchanges around the world. Past FASB chairman Dennis Beresford recently commented on the great strength of U.S. standards (see "Beresford Looks Forward," (/issues/1997/jul/beresfrd.html) JofA, July97).

In a world market, investors will have a larger number of investment opportunities. The U.S. audit—once the assumed seal of approval on U.S. public companies—can no longer be taken for granted. Like all other commodities, audits will have to be brand names. The companies whose statements follow U.S. GAAP, and the auditors who mark them with U.S. GAAS, should clearly display on paper and online their endorsement of a world-class process and product.