Harmonization of Turkish Listed Companies’ Financial Statements

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Extensive Summary

Introduction

Financial statements are vital data sources for financial data users. Being utilized as the core resource in a decision-making process, it is a requirement to devise financial statements in accordance with certain specifications. Conceptual Framework for Financial Reporting (KGK, 2011) listed these certain specifications as being relevance, faithful representation, comparability, verifiability, timeliness, and understandability.

Among such specifications, comparability can be secured through the harmonization in accounting practices. Harmonization refers to analogous accounting practices adopted by national companies (Don and Thomas, 1995). Application of analogous accounting policies boosts harmonization while there is a decrease in harmonization if that cannot be ensured.

Harmonization is classified as formal harmonization (de jure) and material harmonization (de facto). Securing harmonization via legislative regulations stands for the first harmonization step while the emergence of harmonization in practice stage stands for the second harmonization step (Emenyonu and Adhikari, 1998). Regardless of its cause harmonization reveals itself as disclosure harmonization and measurement harmonization (Canibano and Mora, 2000).

In this paper, harmonization level of public companies with financial statements formats issued by SPK (Capital Market Board of Turkey) is examined. Harmonization with the financial statements formats is not mandated. Hence this kind of harmonization level is only related to material harmonization level.

Another objective of our study is to develop a method applicable to measure the harmonization with the financial statements formats. In this study, harmonization will be attempted to get measured via a method we developed.

Method

The research has been conducted over companies listed in Istanbul Stock Market. As of the research period, the number of public companies is 516. Among these companies finance companies have been excluded from the research. Of the remaining 420 companies, all have been included in the research.
Each company’s end-of-2013 & 2014 year balance sheet and income statements (profit or loss statement for the financial year) have been included within the scope of research. Comprehensive income statements, cash flow statements, and statements of change in equity have not been analyzed. The reason for analyzing profit or loss statements solely is because these statements were identified as the key statement by Uniform Accounting Code and companies are accustomed to complying with this long-established formats. On the other hand, expanding the scope of data seemed redundant since our main objective was to develop a method to measure harmonization only.

the financial statements format issued by SPK is the key foundation for this analysis. Each item in financial statements was individually analyzed; items with spelling mistakes and expressing identical meanings were labeled as harmonious.

Of the issued financial statements, the ratio of harmonization with the formats was computed via below-given formula.

\[ \sum_{i=1}^{n} \frac{1 - \frac{p_i}{f_s}}{n} \]

n = number of companies
p_i = disharmonious financial statement item of company i
f_s = frequency of financial statement items

**Findings and Discussion**

Findings of our analysis have been respectively listed for each year. Harmonization level was computed for the complete set of financial statements as well as for each individual statement individually. With respect to the analyzed period, compliance of the company (or companies) with the maximum and minimum harmonization level has been reported. Harmonization has been distinguished as consolidated and individual financial statements. Financial statement items that exhibited a distinctive harmonization level with the financial statements formats issued by SPK while issued were also measured in terms of quantity to delineate minimum & maximum levels; general average and average ratios of the consolidated & individual statement.

As seen in research findings, once the two financial statements are co-evaluated, harmonization level equates to circa 90%. This ratio manifests the presence of analogy between periods. The presence of high-harmonization level proves that the high number of companies have followed the SPK formats. The same ratio escalates to 92% in individual statements. As detected there is a significantly higher level of harmonization in individual statements when compared to consolidated statements.

As harmonization in financial statements level is analyzed it is detected that average harmonization level income statements are 96%, harmonization level of balance-sheet is 89%, and there has been no change in different years. It surfaces that harmonization level of income statements is, on an average base, above harmonization level of balance-sheet. Among consolidated & individual statements, harmonization level of income statements is higher than harmonization level of balance-sheet. One noticeable finding here is that although harmonization level of income statements is generically higher, difference between maximum & minimum harmonization levels is
higher than balance-sheet. In 2013 difference in income statements was 65% (100%-35%), and 20% (98%-78%) in balance-sheet. In 2014 differences were respectively 50% and 20%. There is not any company/companies having 100% harmonization level in income statements. Also, some company/companies have 35% harmonization level. In 2014 although minimum and maximum harmonization levels got closer, they are yet not to be comparable with the difference in balance-sheet harmonization levels. These findings manifest that although certain companies tend to forsake the formats due to their divergent needs, this incidence was evident in relatively few companies that would not immensely affect the average ratio.

As the harmonization level is analyzed as per main groups of balance-sheet, no shifts were observed in harmonization levels throughout different years. On the basis of each main group, harmonization in individual balance-sheets is higher than consolidated ones. Maximum harmonization level (96%) was measured in equities, and minimum harmonization level was observed in short-term liabilities. Additionally, difference between the minimum and maximum harmonization level (43%) was also observed in short-term liabilities. As regards quantity, the maximum number of different accounts was also opened in this group. In long-term liabilities, harmonization level was 95% and although there was merely 1% fall from the equities, unlike equities, it emerges as the key group with the lowest range of difference between maximum and minimum harmonization levels. This finding can be viewed as evidencing that compared to long-term liabilities transactions equity transactions integrate further divergent transaction types.

Aside from that one reason behind the strong harmonization with the financial statement formats is that the formats were devised in minute details. The formats include financial statement items significantly above minimum financial statement items that were specified in TMS 1 provisions. This reality surfaces as one factor diminishing the needs of companies to open individual accounts. As per TMS 1 provisions (TMS 1 par.54), quality is sufficient enough to open two individual account groups in equities while in the formats 17 financial statement items are listed. This deduction is verified by the findings of our research in which maximum harmonization was measured in equities.

Findings of our research are consistent with the findings of the study conducted by Karapınar and Zaif (2008). In their study focusing singly on income statement accounts, it was identified that 22% of companies fully harmonized with the formats, and they even reported items that were nonexistent in their system just because they were listed in the formats. Our study verifies that compliance with the formats continues as of 2008-dated study of Karapınar and Zaif.

It would be of use to illuminate the reasons behind compliance with legal regulations. It has long been argued that accounting practices historically diverged among different states (Nobes, 2002; Bloom,1997) and that accounting was a crucial function of any national culture (Leonard et al., 2010). Traditionally Turkish accounting practices were steered by France and Germany. Accounts chart application as the common trait of Continental Europe States has since then become a cultural aspect of Turkey. Despite the surge of American effects as of the 1960s and recent attempts to fulfill International Accounting Standards, cultural roots still demonstrate compliance with the financial statement formats.
Hofstede (1980 cited in Askary et al., 2008) conducted studies on Turkey’s socio-cultural values and classified Turkey as a state with poor individuality and masculinity traits; with a higher disposition to avoid the ambiguity and with a strong power distance. Relatively low ratios in disposition to avoid the ambiguity and power distance are viewed as indicators of any legal-control focused society (Askary et al., 2008). Gray (1988) utilized Hofstede’s (1980) cultural differentiation to illustrate international accounting differences. The scholar categorized the group Turkey belonged to as representing a strongly-uniformed and legal-control focused accounting system.

Askary et al. (2008) employed a research on the effects of cultural values on accounting practices in Turkey. The research concluded the evidence of positive correlation between high power distance & avoidance from ambiguity and low individuality & uniformed accounting. Findings of our research likewise echo the results of Hofstede (1980) and also Askary et al. (2008) studies. We have testified that in the field of accounting submission to authority is a continued habit, which inevitably gives rise to the emergence of uniformity. This finding demonstrates that “uniformity in reports” expectation underpinned by KGK (Public Oversight Board) has been truly actualized.

In the supervision process, it would be of use for regulatory authorities viz. KGK and SPK to take this cultural effect into account. Perceiving any regulation issued as information and comment purposes only as a mandate may emerge as one factor distancing companies from the philosophy of realistic disclosure of TMS /TFRS (Turkish Accounting Standards/Turkish Financial Reporting Standards). This misperception would inevitably enforce the consecutive step and require the enforcement of further comprehensive and binding regulations.

Results

Our study aimed to measure material harmonization level of public companies with the financial statement formats issued by SPK on the basis of disclosure harmonization. Collected results can be listed as below:

- There is a significantly high level of harmonization with the formats.
- Harmonization level of income statements is significantly above harmonization level of balance-sheet.
- In equity group, harmonization level is significantly above of all the other financial statement groups.
- In balance-sheet minimum harmonization, level is measured in short-term liabilities.
- Harmonization level of individual financial statements is significantly above consolidated financial statements.
- Not any significant changes were detected in harmonization levels among different years.

Obtained findings are deemed to be consistent with cultural codes of Turkey. Social characteristics of Turkey as a legal-control focused society can be detected in the field of accounting too. These results validate that regulatory authorities have reached their aim of ensuring uniformity in financial statements. Nevertheless, it would be for the benefit of regulatory authorities to take action by following such cultural codes.
Otherwise, they would be disposed to depart from the core spirit of TMS/TFRS and feel mandated to regulate and annotate all details.

Our study mainly focused on balance sheets and income statements. Comprehensive income statements, cash flow statements and statements of chance in equity have not been analyzed.