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Financial Statement Framework for Multinational Companies, Preparation, Translation and Analytical Issues: A Critique

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ABSTRACT
This study focused on critiquing the framework for financial statements of multi-national companies (MNCs), translation and analytical issues. To achieve this, some extant literature on Generally Accepted Accounting Principles (GAAPs) as well as environment factors and accounting system affecting MNCs were examined. This paper presented the issues that besiege the MNCs: issues that border on the inability to develop internationally recognized accounting standards for MNCs. Nevertheless, some reforms were made, that would allow the MNC, s users of MNCs' financial statements and investors make informed investment and business decisions on the basis of reports that are comparable across the globe. Such reforms presented include an advocacy for a sustainable global framework and regional mutual agreements that could be reached on the basis of defined similarities in accounting systems that may exist amongst these companies, among others.
Key word: Framework Environment Factor GAAP, MNCs, Financial Reporting.

1.0. INTRODUCTION

Multi-National Companies (MNCs) have become veritable and most vital instruments and institutions for economic development, social change, technology, dynamism and in essence, new ideas (Singh, 1998)). MNCs operate within the contexts of environmental variables in locations other than their home-base countries. MNCs in Nigeria have their origin in locations other than Nigeria but subject beside the variables in their home countries, to variables in Nigeria. By definitions or description by Walton, Haller and Raffournier (1998), MNCs are a form of collection of autonomous operating units under a distant control. Such operation units, according to Odusola (2002) are foreign direct investments, and to that extent, a growth-enhancing factor in the developing countries. The concept of MNCs is extended to describe a relationship similar to the parent and subsidiary form in which the parent company operates beyond the shores of the home country through affiliates in another country for activities involving the production of goods and services (Frank, 1989).

According to Owojori and Asaori (2010), the MNCs, though transnational in nature, is usually tested by their ability to control more than thirty (30%) percent of the global gross products outside their home countries. This definition presupposes that a MNC cannot be so described if the parent group cannot control thirty (30%) percent and above of the global gross products. However, what is of interest is that the MNCs operate in countries other than their countries of origin. To this end, it is reasoned to think that MNCs are unlikely the same in terms of sizes, types, forms, complexities, and functions. In addition, the controls exercised over these companies are still shrouded in controversy in accounting literature (Mintzberg, 1979).

In addition, the challenges posed by the environment where the MNCs companies as well as the changes therein tend to affect the central control activities over the MNCs. Besides, there is an interplay of subsisting framework in Nigeria where the MNCs operate and that of the home countries of these companies. The Nigerian Generally Accepted Accounting Principles (GAAPs) and the versions of GAAPs in other countries tend to impinge on the activities of MNCs in Nigeria.

There is no doubt, thus, that the Nigerian MNCs operate in complex and challenging environments ranging from the legal, political, cultural, technological and economic influences, among others. This myriad of challenges, bordering on subsisting frameworks and other challenges, lead to accounting practices that capture the MNCs framework in place. Arguments are ubiquitous that the U.S. GAAPs are used by the U.S. MNCs in Nigeria while, Nigerian companies are compelled to use Nigerian GAAPs. The implication of these "conflicts" is the production of multiple accounting reports which may be designed to serve various governments-the home and host countries (Nobes and Parker, 1991). According to Igbal, Melcher and Elmallah (1997), given the multiplicity of reports, foreign investors may have to contend with understanding the content of the financial statements of the MNCs.Generally noted, diversity in GAAPs tend to affect the MNCs if the quest for capital expansion and the need to raise capital in their countries of operation is anything to go by.

It is against the aforementioned submissions that this paper is written, to attempt a critical appraisal of the MNCs framework that forms the basis of financial statements preparation, translation and analytical issues.

2.0 ACCOUNTING AND ACCOUNTING SYSTEM OF MNCS

Accounting as a business language, has been recognized globally. It transcends national bounds. Accounting hinges on its ability to identify measure and interpret financial and economic variables to permit informed judgments (Adeniyi, 2008; Paul, 2009). Accounting does not have territorial bounds and therefore it is used to communicate the activities, existence and the evolution of the financial positions and performances of economic entities.MNCs activities are conducted in locations other than their home countries, and are therefore exposed to the environment of their host countries. According to Owojori and Asaolu (2010), the many-sided activities of the MNC lead to a lot of activities reflected in the accounting system. Foremost among the activities, are the mechanisms and methodology of seeking cross border quotations on various stock exchanges and transnational financing activities. These activities entail the ability to capture the special information needs of creditors and investors all around the world.

The accounting systems of MNCs are complex and somewhat difficult to manage because of the inter-connection and web of relationships with other companies and locations which lead to the production of financial reports. The MNCs have accounting systems whose responsibility it is to produce financial statements which reflect a true situation of transactions captured in the system. Such a system can be very multifaceted; problems relating to the preparation of international operation occur because businesses with transactions in more than one country have to deal with more than one currency, accounting principles and reporting practices of different countries. Given these scenarios, the system concept of accounting of MNCs is very crucial considering the environment they operate.

2.1. National generally accepted accounting principles (GAAPS)

GAAPs are a collection of methods used to process, prepare and present public accounting information. GAAPs are, on the whole, very general in their methods, as they need to be somewhat applicable to many types of industries. GAAPs can be principle – based or based on specific technical requirement. Due to the fact that, in many instances, GAAPs are flexible and general, most industries in the U.S or in the U.K are expected to follow the GAAP principles in such countries. Nigerian GAAPs effectively are used by Nigerian companies such that foreign investors find it difficult to figure out issues that have to do with them because there are no disclosure requirements for them. According to Ededegbe (2009), companies in Nigeria are subject to Nigerian GAAPs but are not confined to particular national GAAPs.

GAAPs are a product of different stakeholders and organizations. In the U.S, the Financial Accounting Standard Board contributes to the U.S GAAP just as the Nigerian Accounting Standard Board Contributes to the Nigerian GAAP. GAAPs across countries vary but based on few basic principles of *relevance, understandability comparability and consistency* (Marlins-Kuye, 2010).

Consistency

This principle states that all information should be grouped and presented the same across all periods .According to Lewis and Pendrill (1996), Consistency requires that the measurement and display of the financial effects of like transactions and other events be carried out in a consistent way within each accounting period and from one period to the next, and in a consistent way by different entities. However, according to this principle, undue rigidity should be avoided in the event of a new accounting policy more appropriate to the circumstances of the entities. Users, in the event of a change of this policy, are made aware of the change.

For a MNC, the method used for any accounting item or any accounting treatment will be reflected in various accounting or financial statements in both the home and host countries. While the U.S GAAP favours the use of *last in first out*, the Nigerian GAAP favours the use of *first in first out,* both methods, originating from different GAAPs.

Relevance

This principle suggests that information presented in financial statement and other public statements should be appropriate and assist the user to evaluate the statements to make educated guesses about the future state of the entity. The Accounting Standard Board Draft principle on Relevance states that financial information contained in the financial statement is useful to the user of the financial statement if the information has the ability to influence the decisions of users by helping them evaluate past, present or future events or confirm or correct their past evaluation.
The MNCs financial statements, therefore, should contain information that is relevant and useful to the users to make informed judgments. This principle also presupposes diverse users which cut across national bounds.

Reliability

This means that information contained in the financial statements must tell the truth, the whole truth; the information must be comprehensive and verifiable (Solomons, 1989); and such verifiability must be undertaken by an independent party. According to the Accounting Standard Board (1995), information contained in the financial statement has the quality or reliability when it is free from material error and bias and can be depended upon by users to represent faithfully what it either purports to represent or could reasonably be expected to represent.
Following this GAAP, therefore, suggests that the company is representing a clear picture of what really happened and is happening with the company.

Comparability

Lewis and Pendrill (1996) identify two aspects of comparability. This includes: the ability of users to compare the results of entity overtime, and to compare the results of different entities. The former is termed time series analysis while the latter is seen as cross sectional analysis.
Comparability is one of the most important GAAPs categories. A company's financials and other documentation can be compared to similar business within its industry. This GAAP is so important such that without effective and meaningful comparisons between companies and within industry to benchmark how a company is doing compared to its peers, potential investors may be unable to come to meaningful decision. This GAAP ensures that all companies, whether MNCs or not, are on the same level playing field and that the information they represent is consistently relevant, reliable and comparable.
Based on the scenario described, it is interim clear that no GAAP can have universal application beyond the GAAP principles of relevance, understandability comparability and consistency. The Nigerian GAAPs are applicable to Nigerian companies, including the MNCs. Other countries have their own versions of GAAPs that are similar in purpose, although not always in design (Bradford, 2007). However, according to Bangudu (2009), Nigerian GAAPs are mandatory for Nigerian companies, although Nigerian banks with overseas subsidiaries are having to report under the international financial reporting standard, (IFRS) in certain markets, like Ghana, the U.K. the U.S. and South Africa.

2.2 Environmental factors and the choice of GAAPs

Quite dearly, countries including Nigeria, do not adopt particular accounting standards, or GAAPs for their sake. Accounting standards or GAAPs represent or reflect several major environmental variables that impinge on their formulation. Principle among which are;

The nature of creditors – company relationship

According to Mueller, Gernon and Meek (1997), the country fits into three different relationship patterns. However, in all, the financial statements are oriented towards the information needs of a relationship that is large and powerful. Where the country has larger creditors – investor group, the needs of this group are likely going to be packaged through the orientation of the financial statements of the MNCs. The widespread ownership is usually uninvolved in the day-to-day running of the company. To this end, the objective of the financial statements is to describe the financial position and financial performance intended to assist investors and creditors to make sound economic decisions. Examples are the U.S and the U.K.

Satisfaction of capital needs of small number of large financial institutions

The criticality of personal contacts in a banking relationship has influenced the protection of the creditors through financial reports oriented towards their information needs. This is particularly the case in Japan and Germany. This point presupposes that financial reports tend to suit a financing institution to satisfy the capital needs of that company.

Level of inflation

The inflationary trends determine the development of reporting standards. In the U.S. where the inflationary trends are minimal, it uses the historical cost accounting as a measurement basis. If a country has experienced significant inflation, the historical cost principle may be adjusted; or better still, the current cost or value accounting becomes appropriate cost or value .In addition, when examining a country's business environment in which a MNC operates and for which the financial statements are met, the size and complexity of businesses must be considered. Besides, the sophistication of the management and financial community and the overall general levels of education as well as the user's sensitivity to the use of financial statement may be also considered. Where the users' sensitivity to the use of financial statement is low, the demand for sophisticated set at financial statement will be low.

Cultural milieu

Cultural background has been known to affect the accounting development. Carr, Brinker and Sherman (2) acknowledge the inconclusive debates on the relationship between culture and development of accounting. However, accounting research attempts to link culture to components of accounting concepts, standards and practices. To this end, diversity in accounting practices is acknowledged, considering the diversity in culture and the development of national standards. Besides, individual countries are known to be diversified in races, religions and geographical locale.

2.3. Criticism of national GAAPS

No one national GAAPs suffice; national GAAPs reflect cultural, racial, religious and geographical diversities. GAAPs or different GAAPs affect corporate managements of MNCS in several ways.

Production of multiple financial reports

Different sets of financial statements must be prepared in accordance with each country's standards, which is costly. MNCs also sense that accounting diversity affects competitiveness. Yet, MNCs are expected to issue financial statements that reflect national GAAPs and securities regulation, thereby limiting the possibility of raising capital beyond their countries of operation. Such 'unequalness' in national GAAPs and the differences that accompany them, make it difficult for MNCs not just to acquire, dispose or operate, but creates an unlevel playing field.

Limitations of international investment opportunities.

National GAAPs limit international investment opportunities existing beyond national confines. Global investment is difficult when international investors cannot understand and appreciate the contents and basis of the preparation of financial statements. Beyond the realms of financial reporting, investment analysts confronted with diversities in accounting and GAAPs are at a loss, and the natural consequence is inefficiency of financial markets.

Loss of activities in stock markets

Stock markets are inactive to the extent of non-listing of companies on their exchange because of diversity in GAAP. Accounting and requirements vary extensively for listing a company on a foreign stock exchange (Salter and Kantor, 1996). Besides, companies may be reluctant to incur additional cost of preparing multiple financial reports to reflect the plethora of changes necessary to list on a foreign stock exchange.

Reluctance by professional accountants and other consultants

National GAAPs tend to favour professional accountants and other consultants who see the diversity in GAAPs as a favourable development earn higher audit and consulting fees. This is because diversity in GAAPs tends to complicate cross border auditing and possibly consulting

It is instructive to note that, despite the criticisms discussed above, no internationally recognized standards of accounting exist today; and principal problems and challenges impede the development of internationally recognized accounting standards. Ezejuele (2001) list them as: the failure of accountants or users to agree on the objective of financial statement; differences in extent to which accounting profession has developed in various countries; influence of tax laws on financial reporting; provision of companies laws in various countries; requirements of government and other regulatory bodies; diversity in environmental factors in various countries; inconsistencies in accounting practices recommended by accounting professions in different countries;

3.0. TRANSLATION AND ANALYTICAL ISSUES IN FINANCIAL STATEMENT OF MNCS

The accounting systems of MNCs reflect operation, management and accounting of business and activities in more than one country. So the accounting system is complex because of the problems relating to the preparation of financial statements of MNCs.

Issues and problems in MNCs relate to managing and accounting for businesses with transactions in more their one country. The issues of more than one currency, accounting principles and reporting practices still subsist. In respect of financial reporting, it is significant to know which financial reporting requirements are to be applied; hence the issue of ownership or whereabouts of the headquarters become important. Issues of measurement of assets and liabilities and the values thereof for balance sheet purposes are central in MNCs financials.

Conceptual issues in the definition of MNCS

MNCs and TNCs (transnational companies) have been used interchangeably. But the two concepts have been defined differently (Freeman and Persen, 1981 and Frank, 1981). And yet economists are yet to resolve the definitional problem in the concept of MNC. The economist sees MNC as a company that: engages in foreign production through its affiliates located in several countries; exercises direct and distant control over the policies of its affiliates and implements business strategies in production, marketing, finance and staffing that transcend national boundaries.

Location of ownership of MNCs

For the purpose of accounting for the operation of MNCs, various criteria have been suggested to locate ownership of MNCs. For financial reporting purposes, it is unclear which financial reporting requirements may be applied. Therefore ownership or headquarters of MNC is undefined. Issues that arise include how transactions in different currencies arising from the multinational relationship of MNCs are to be treated; what measures of assets and liabilities are appropriate for balance sheet reporting and what methods and processes of consolidation are to be used

Foreign exchange translation

Issues of foreign exchange translation relate to the mechanism used to translate foreign currency balances to domestic currency equivalents. At what rate should a transaction be translated? For balance sheet purposes, method of (i) the current rate method (ii) current-noncurrent (iii) the monetary nonmonetary method and (iv) the temporal method are available with their strengths and criticisms. Given the fluctuations in exchanges rates, divergence in results and the range of dissimilarity in exposure, using different methods, the U.S and the U.K and Canada make pronouncements on the use of temporal method.

Yet the temporal method assumes the use of historic cost or the current rate basis for all accounts balances. This may not be realistic because the exchange rate of the time of transaction may be different at the exchange rate of financial report. Beside what would be the basis of depreciating a long term assets that have been held. Through firm tend to minimize fluctuation in exchange rate to reduce the possibility of loss on the foreign currency involved in the original transaction, the problem is how to account for the benefits and/ or cost arising from hedging activates. Besides, overseas operations, as distinct from normal operation of the companies, pose a problem in terms of accounting for such overseas operations or transactions.

Costing procedures issue

How does an MNC reconcile a costing procedure or method that minimizes profits and the operation of the company in a developing country? While developing countries, including Nigeria, have no transfer pricing regulations, the MNCs operating in the country rely on guidelines or regulations from their home countries. In most cases such guidelines tend to favour as such transfer pricing methods tilt towards minimizing their tax liabilities.

4.0 REFORMS IN FRAMEWORK FOR MNC FINANCIAL REPORTING SYSTEM

The frameworks for MNCs' financial statements demand that it is adjusted to reflect the stark realities which are on ground. The following are suggested to improve the framework and by extension financial reporting.

Countries with similar accounting systems should collaborate

When countries have similar accounting system because of history and relationships, the regulations can work on bilateral or multilateral level. This can strengthen mutual recognition of each other's accounting standards. This will facilitate multinational offerings by MNCs companies. In Nigeria with similar history with other Anglo-phone countries, similar accounting system could enhance the operation and financial reporting of MNCs. In addition if the accounting system of MNCs will be effective, the management teams across the MNCs should be those who can break cultural barriers; those who release their multi-skills to reflect global views of multi-country, multifunctional and multi-faceted activities in the international business.

Proactive approach by MNCs

The globalization of business, the dynamism and changes in the environment, ranging from changes in the legal, economic political and diversity in culture requires fresh and proactive approach by the MNC to remain relevant.

Adoption of global accounting framework

In addition an adoption of global accounting framework for the preparation of financial statements for MNCs and by extension world countries is advocated. Such global accounting framework should be principle-based to reflect true economic substance of transaction as opposed to the letter of law (Shortridge, 2004). With global accounting framework, national GAAP will be subsumed in global or harmonized GAAPs. There is need for a global framework in order to help the foreign investors not just to ease the understanding of the financial statements of the MNCs but to help aid the preparation of financial statements of the foreign companies.

Clear definition of the concept of MNCs.

MNCs should been specifically defined to minimize conceptual misinterpretation of MNCs. This will involve a conceptual redefinition of the framework and the various criteria, such as location of ownership, orientation (home country; host country or world), or other features. This is to enable the MNCs situate the final financial reporting and the financial reporting requirements. In addition, MNCs would develop common reporting system (KPMG, 2008) that could streamline their reporting and reduce the cost of producing multiple financial reports.

***Close monitoring of consolidation rules where the MNCs operate*.**

One of the tasks associated with accounting for MNCs is to prepare its consolidated financial statements. Consolidated financial statement requires the combination of the financial statement of entities, whether subsidiaries or not, within the same group but in different countries. It is advocated that the course of consolidation, the rules, standards and practices, prevailing in the countries where the MNCs operate, be closely followed and monitored.

5.0 CONCLUSION

This paper focuses on "critiquing the framework of financial statements of MNCs, preparation, translation and analytical issues". This has been achieved by examining the GAAPs, environmental factors and accounting system that guide the MNCs operation and form the basis of financial statements. Financial accounting system and financial reports in the world are reflections of their environments in which diversities in culture and accounting practices exist. As MNCs conduct business in locations other than their home base countries, a common platform for these companies is required. But the challenges are there. The world business environment demands for principles-based framework and enforcement of a common global accounting system, and collaboration amongst countries with similar accounting systems, that would allow the MNCs users and investors to flourish. This can be achieved in the context of making informed investment and business decisions, and utilizing reports that are comparable across the globe. These decisions will include unhindered foreign direct investment and global expansion.

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