

Sociocultural IFRS Value Analysis in Five Balkan Countries

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The Balkan region of the Central and Eastern European countries (CEEC) includes many emerging economies formerly under Soviet Union influence. Bulgaria, Croatia, Romania, Serbia and Slovenia were selected for this study. These countries previously experienced the influence of other powerful neighbors, including the Austria based Holy Roman Empire and the Turkish Ottoman Empire. Many have also been influenced culturally by nearby Italy and Greece. This paper examines the sociocultural potential of each country to establish and sustain sufficiently high quality financial reporting to support continued economic growth and an appropriate allocation of international capital. The analysis is based on previous research into cultural accounting value methods. That research examined Hofstede cultural value dimensions and corresponding Gray accounting value dimensions to develop country specific accounting value profiles that are compared with a posited ideal IFRS favorable accounting value profile. Other research has quantified a country's sociocultural IFRS orientation using a Composite IFRS Orientation Index and an Expanded IFRS Orientation Index. The latter incorporates additional sociocultural factors of perceived corruption, political risk, educational level, and regulatory business orientation. Opportunities for the improvement of financial reporting and the financial reporting infrastructure of these countries are discussed.

INTRODUCTION

Bulgaria, Croatia, Romania, Serbia and Slovenia share a common geographic affinity as countries in the Balkan region. Similarities do not end there, however, as they all experienced, to a greater or lesser degree, a long period of political and religious subjugation under Turkish Ottoman rule. The influence of this period can still be seen in Turkish influence in music and dress, as well as, the presence of indigenous Muslim populations. All of these countries, except Bulgaria, escaped Ottoman rule and became part of the Austro-Hungarian Empire, which itself collapsed with World War I. After a period of German occupation during World War II, they all fell under the strong influence of Soviet Russia and remained in the Socialist Eastern Block until the dissolution of the Soviet Union.

Within this common experience, there are specific factors that distinguish these countries from one another, sometimes creating affinities and disaffinities to one another or to outside neighbors. One such factor is religion. Prior to the introduction of Islam from the Turks, the primary religion was Roman Catholic in the western side of the Region, and the Eastern Orthodox religion in the eastern side. Of the five countries selected for this study, Slovenia and Croatia are predominantly Roman Catholic, while Bulgaria, Serbia and Romania are predominantly Eastern Orthodox. Catholicism naturally predominates in Croatia and Slovenia, given their proximity to Catholic Austria and Italy. Religion has had a powerful divisive effect on the relationship between Croatia and Serbia, in spite of the fact that both nations speak

the same language, albeit using different alphabets. Language is the other curious factor in this group. Serbo-Croatian, or as the Croats like to call it Croato-Serbian, is a south Slavic language, as are the languages of Bulgaria and Slovenia. They are all closer to Russian than to any of the western European languages. The only non-Slavic language in the group is Romanian, the most eastern member of the Romance language group, which includes Italian, Spanish, Portuguese and French. Historically, Eastern Orthodox Russia has claimed a strong allegiance to the Orthodox peoples of the Balkans and particularly to the Slavic Serbs. Even in recent times, signs could be found in Moscow with the words “Holy Russia and Serbia,” a phrase which goes back to Czarist efforts to free Serbia from Ottoman rule. Today such phrases reflect a right-wing rejection of non-Orthodox western influences and, perhaps, an affinity based on the overlay of religious, linguistic and historical ties, including a sense of shared Soviet experience.

Important neighboring states frequently influence some or all of these countries culturally, politically and economically. Five neighbors are identified: (a) Austria and Italy to the west, (b) Russia to the east, and (c) Greece and Turkey from within the Balkan region. These countries serve as useful points of comparison in our analysis of cultural accounting values of the study group. The United States is also cited for comparison, as it is representative of cultural values much more closely in harmony with IFRS reporting standards.

Advancement of Accounting and IFRS in modern Bulgaria, Croatia, Romania, Serbia and Slovenia has been closely aligned with the successful transition of these countries into members of the European Union (EU). All but Serbia are now member states and, Serbia is completing the candidate process for membership. From 2005, adoption of IFRS for financial reporting of large public companies has been a requirement for EU members and an important milestone for obtaining EU membership for the Eastern bloc countries. As indicated in Table 1, all of the countries state that they require all listed consolidated companies to use IFRS for financial reporting. (PWC, 2013)

TABLE 1
IS IFRS REQUIRED OR PERMITTED FOR LISTED COMPANIES?

Country	IFRS required or permitted for listed companies?
Bulgaria	Required for consolidated and standalone/separate financial statements - IFRS as adopted by the EU
Croatia	IFRS required for listed companies, financial and large unlisted companies, permitted for others -IFRS as adopted by the EU
Romania	Required for Consolidated/ standalone just for banks - IFRS as adopted by the EU
Serbia	Required for consolidated and standalone/separate financial statements - IFRS as adopted by EU (possible version translation lags
Slovenia	Required for listed entities as adopted by the EU

All these countries are, however, new to the IFRS implementation process and have until recent times utilized communist state plan accounting systems. Jerman and Novak cite Slovenia code law tradition and strong linkage between financial accounting and tax laws in Slovenian accounting, noting that most companies, except for the few large stock companies, still do not use IFRS and that there is a lack of studies on IFRS compliance. (Jerman & Novak, 2014) Similar observations can be found regarding the other Balkan countries in this study.(Albu & Albu, 2012)(Ovidiu, 2011)(Plaats & Nagy, 2011)(Barac & Klepo, 2006)Although the largest companies can rely on the services of the large international accounting firms, the real challenge for IFRS implementation is to ensure that local company accounting and auditing firms will be able to embody the values of IFRS in their practice.

STATEMENT OF PURPOSE

This paper examines the relative potential of Bulgaria, Croatia, Romania, Serbia and Slovenia to establish and maintain sufficiently high quality financial reporting based on an evaluation using two quantitative measures: the Composite IFRS Orientation Index, and the Expanded IFRS Orientation Index. These were developed by the author in a recent study. (Borker, 2014) These measures are determined by a quantitative analysis of each country's culturally derived accounting values as they relate to IFRS. Four of these accounting values are taken from Sidney Gray's accounting value dimensions -- Conservatism, Uniformity, Professionalism, and Secrecy. (Gray, 1988) To these, a fifth value dimension, Stewardship, is added by the author, based a set of selected sociocultural factors. The aim of the analysis is to understand the cultural ease with which these countries will adapt to IFRS relative to one another and to countries outside the Baltic countries, to gain regional and country specific insights into strengths and opportunities for improvement. In addition, this paper continues testing the measurement methodology by applying it to the specific regional and country contexts of the Balkan States.

THE LITERATURE REVIEW

In the early Eighties, Geert Hofstede published his first book on cultural value dimensions worldwide. He reported index scores for individual countries for four cultural dimensions: Power Distance (PDI), Individualism (IDV), Masculinity (MAS) and Uncertainty Avoidance (UAI). (Hofstede, 1980) Subsequently, Hofstede developed additional cultural dimensions including Long-Term Orientation (LTO) and Indulgence vs. Restraint (IVR). (Hofstede, 2001)(Hofstede, Hofstede, & Minkov, 2010) These dimensions are fully described on the official Hofstede website. (Hofstede, 2013)

Subsequent to the appearance of first Hofstede volume on cultural value dimensions, Gray published a paper in which he posited a relationship between Hofstede individual country cultural value dimensions and a set of accounting value dimensions. Gray identified four accounting dimensions, Conservatism (opposite of Optimism), Uniformity (opposite Flexibility), Professionalism (opposite Statutory Control) and Secrecy (opposite Transparency) (Gray, 1988). He related these accounting dimensions to Hofstede cultural dimension in the form of four hypotheses shown in Table 2.

TABLE 2
GRAY'S FOUR HYPOTHESES

H1	The higher a country ranks in terms of individualism and the lower it ranks in terms of uncertainty avoidance and power distance then the more likely it is to rank highly in terms of professionalism.
H2	The higher a country ranks in terms of uncertainty avoidance and power distance and the lower it ranks in terms of individualism then the more likely it is to rank highly in terms of uniformity.
H3	The higher a country ranks in terms of uncertainty avoidance and the lower it ranks in terms of individualism and masculinity then the more likely it is to rank highly in terms of conservatism.
H4	The higher a country ranks in terms of uncertainty avoidance and power distance and the lower it ranks in terms of individualism and masculinity then the more likely it is to rank highly in terms of secrecy.

Gray qualifies his hypotheses with observations regarding the relative importance of various Hofstede dimensions in relation to his accounting dimensions. For example, in discussing Professionalism, Gray noted that Hofstede's IDV and UAI are strongly linked to his Professionalism value; while PDI is linked, but not as strongly, to the Professionalism value.

In recent years, Braun and Rodriguez quantified each of Gray's four accounting dimensions for individual countries by taking a simple average of scores for the corresponding Hofstede dimensions. (Braun & Rodriguez, 2008) In the case of dimension scores that have a negative or inverse relationship to a Gray accounting dimension, the Hofstede score is adjusted in the following manner. The mean score for that dimension for the total countries analyzed is subtracted from the specific country's score. Next, this

value is multiplied by -1, and then added to the mean score. By using this conversion of negatively correlating Hofstede scores, they were able to create opposite positive scores for each Hofstede dimensional component of a Gray accounting dimension. By using a simple average in their computation, Braun and Rodriguez assume that all Hofstede dimensions that relate to a given Gray dimension should have an equal weight. However, this did not take into consideration Gray's observations that certain Hofstede dimensions have greater or lesser importance than others in determining Gray's dimensions. (Gray, 1988)

In a recent conceptual paper, Borker developed a revised mapping of the relationship between Gray accounting value dimensions and Hofstede cultural value dimensions that provides relative weightings based on Gray's indications in his original article. (Borker, 2013a) Borker also expanded the model to include two Hofstede dimensions identified after the publication of the Gray article. These are Long-term orientation (LTO) and Indulgence versus Restraint (IVR). Table 3 summarizes the positive and negative relationships between Gray and Hofstede dimensions, using '+' to represent a lower weight positive correlation, '+ +' to represent a higher weight positive correlation, and '- 'and '- -' to represent, respectively, lower versus higher weighted negative correlation relationships. Finally '?' is used to represent no, or an uncertain, relationship between the Gray and Hofstede dimensions. The use of these symbols for the first four Hofstede dimensions (see shaded area in Table 3) was intended to reflect Hofstede's own comments in his original article on the greater or lesser importance of certain Hofstede dimensions. The use of these symbols under Hofstede's two added dimensions, LTO and IVR, indicate an assumed relationship between these two dimensions and Gray's four accounting dimensions based on an examination of the Hofstede value dimensions for seven Anglo-American countries.

TABLE 3
EXPANSION OF HOFSTEDE-GRAY RELATIONSHIPS

	Power Distance: PDI	Individualism: IDV	Masculinity: MAS	Uncertainty Avoidance: UAI	Long-Term Orientation: LTO	Indulgence vs. Restraint: IVR
Conservatism	+	-	-	++	+	-
Uniformity	+	--	?	++	+	-
Professionalism	-	++	?	--	-	+
Secrecy	++	--	-	++	+	-

Borker also proposes an IFRS favorable accounting value profile based on Gray accounting dimensions. This profile assumed that the ideal IFRS accounting value profile for a country was one characterized by a low degree of the dimensions Conservatism, Uniformity and Secrecy, and a high degree of the dimension Professionalism. This translates into a profile of Optimism, Flexibility, Professionalism and Transparency. The concept of individual country dimensional profiles and an IFRS favorable profile are applied in several other studies. These include studies of the BRIC countries, emerging economies in Central and Eastern Europe and the 3G economies. (Borker, 2012b)(Borker, 2012c)(Borker, 2013b)

RESEARCH METHODOLOGY

In a subsequent study, a methodology was developed for measuring the level of a country's cultural IFRS orientation through two indices: the Composite IFRS Orientation Index, and the Expanded IFRS Orientation Index. (Borker, 2014) The first of these indices quantifies the level of fit between a given country's accounting cultural values and those of IFRS. The procedure involves first establishing a methodology for quantifying each of Gray's four cultural dimensions for a given country and then adjusting and combining these scores to derive a quantitative measure of the overall level of fit with the

Gray values favorable to IFRS. In developing the Gray dimensional scores, the study employed methods developed by Braun and Rodriguez discussed above. The study developed three alternative versions of Gray value indices: (1) one based on a simple averaging of Hofstede dimensions, (2) another based on a weighted average of the Hofstede first four cultural dimensions as discussed by Gray and (3) one that incorporated two later developed Hofstede dimensions, LTO and IVR. Subsequent tests of these methods have led to the conclusion that the second version is most appropriate for scoring countries using the Composite IFRS Orientation Index.

Another index was developed from the IFRS Orientation Index that incorporated various socio-political factors thought to be associated with the accounting value of Stewardship, a value not included in Gray's original dimensions. This second index is the Expanded IFRS Orientation Index. It is determined by taking a weighted average of the Composite IFRS Orientation Index, weighted at 80% plus scores for four sociocultural indices each weighted 5%. The indices are: (a) The Corruption Perception Index (CPI) provided by Transparency International, (Transparency International, 2013), (b) an adaptation of AON's political risk ratings by which the higher a country's political risk, the lower the score it receives, (AON, 2013), (c) the United Nation's Education Index adjusted for inequalities, (Malik, 2013), and (d) the World Bank's Regulatory Index. (World Bank, 2013)

The present study applies the above methodology for determining a country's Composite IFRS Orientation Index and Expanded IFRS Orientation Index discussed above, to each of the five Balkan countries investigated.

RESULTS AND ANALYSIS

Hofstede cultural dimension scores are provided for Bulgaria, Croatia, Romania, Serbia and Slovenia and selected other countries in Table 4.

TABLE 4
HOFSTEDE CULTURAL VALUES BY COUNTRY

	PDI	IDV	MAS	UAI	LTO	IVR
Balkan States:						
Bulgaria	70	30	40	85	69	16
Croatia	73	33	40	80	58	33
Romania	90	30	42	90	52	20
Serbia	86	25	43	92	52	28
Slovenia	71	27	19	88	49	48
Neighboring States:						
Austria	41	44	70	35	41	44
Italy	48	45	69	43	48	45
Russia	79	76	38	77	79	76
Greece	76	78	36	70	76	78
Turkey	68	68	46	65	68	68
Other Important States:						
United States	40	91	62	46	26	68

Table 5 shows Gray accounting value dimensions calculated for each country based on B weightings of the Hofstede cultural dimension scores. For comparative purposes, Gray dimension scores for the United States are provided.

TABLE 5
GRAY ACCOUNTING DIMENSION SCORES BY COUNTRY

Gray Dimension Scores Based on Weighted Average of Four Hofstede Dimensions				
	Conservatism	Uniformity	Professionalism	Secrecy
Baltic States:				
Bulgaria	71	71	43	69
Croatia	69	69	45	68
Romania	77	77	37	76
Serbia	78	79	35	77
Slovenia	77	74	40	74
Neighboring States:				
Austria	41	44	70	35
Italy	48	45	69	43
Russia	79	76	38	77
Greece	76	78	36	70
Turkey	68	68	46	65
Other Important States:				
United States	33	25	89	29

Composite IFRS Scores are calculated for each country based on the Gray dimension scores above which have been adjusted for dimensions with a negative relationship to IFRS orientation. These are presented in Table 6.

TABLE 6
COMPOSITE IFRS ORIENTATION INDEX BY COUNTRY

Composite IFRS Orientation Index Derived per Formula					
	Conservatism	Uniformity	Professionalism	Secrecy	Composite IFRS Orientation Index
Balkan States:					
Bulgaria	44	42	43	43	43
Croatia	46	44	45	44	45
Romania	38	36	37	36	37
Serbia	37	34	35	35	35
Slovenia	38	39	40	38	39
Neighboring States:					
Austria	74	70	70	76	73
Italy	67	68	69	69	68
Russia	36	37	38	35	36
Greece	39	35	36	42	38
Turkey	47	45	46	46	46
Other Important States:					
United States	82	88	89	83	85

Table 7 provides the ranked list by country of Composite IFRS Orientation Index scores. Balkan States are bolded.

TABLE 7
COMPOSITE IFRS ORIENTATION INDEX SCORES BY MAGNITUDE

Rank	Country	Composite IFRS Orientation Index
1	United States	85
2	Austria	73
3	Italy	68
4	Turkey	46
5	Croatia	45
6	Bulgaria	43
7	Slovenia	39
8	Greece	38
9	Romania	37
10	Russia	36
11	Serbia	35

The Composite IFRS Orientation Index is combined with four additional sociocultural factors to produce the Expanded IFRS Orientation Index as shown in Table 8.

TABLE 8
EXPANDED IFRS ORIENTATION INDEX SCORES BY COUNTRY

Expanded IFRS Orientation Index based on Weighted Average of Composite IFRS Orientation Index and Four Additional Factors						
	Composite IFRS Orientation Index	Corruption	Political Risk	Education	Regulation Index	Expanded IFRS Orientation Index
	80% weight	5% weight	5% weight	5% weight	5% weight	100%
Balkan States:						
Bulgaria	43	44	70	76	55	46
Croatia	45	49	50	70	41	46
Romania	37	47	70	78	74	43
Serbia	35	42	30	71	40	37
Slovenia	39	66	90	91	78	47
Neighboring States:						
Austria	73	74	90	84	82	75
Italy	68	45	90	74	50	68
Russia	36	30	50	78	21	38
Greece	38	39	90	76	46	43
Turkey	46	53	90	44	51	49
Other Important States:						
United States	85	78	90	94	101	86

Table 9 lists these countries in order of the magnitude of the Expanded IFRS Orientation Index scores. Balkan States are in bold.

TABLE 9
EXPANDED IFRS ORIENTATION INDEX SCORES BY MAGNITUDE

Rank	Country	Expanded IFRS Orientation Index
1	United States	86
2	Austria	75
3	Italy	68
4	Turkey	49
5	Slovenia	47
6	Croatia	46
6	Bulgaria	46
8	Greece	43
8	Romania	43
10	Russia	38
11	Serbia	37

DISCUSSION

On the Composite IFRS Orientation Index (CIOI), all the Balkan countries are below 50 and within 10 points of one another. Bulgaria and Croatia are at the high end of the range at 45 and 43, while Serbia and Romania are at the low end at 35 and 37, respectively. Slovenia, at 39 is in the middle. These scores are consistent with the component score levels for all the Gray accounting values of each country. Looking at comparisons with outside countries, we find that all five countries have composite IFRS scores that are much closer to their Balkan neighbors Greece (38) and Turkey (46) and to their eastern neighbor Russia (36) than to their Western European neighbors, i.e., Austria (73) and Italy (68), or to the United States (85). Specifically, Croatia and Bulgaria have scores closest to Turkey, the highest scoring Balkan neighbor, while Serbia and Romania are closest to Russia and Greece. All five countries have scores well below their western neighbors or the United States. They are separated from their lowest scoring western neighbor Italy by a minimum of 23 points.

On the Expanded IFRS Orientation Index (EIOI), all countries are still below 50 and within 10 points of each other, but with a clear divide between the four current EU member states ranging from 47 to 43 (4 point spread) and Serbia at 37. Slovenia, at 47, ranks highest on this index. Slovenia's high ranking on EIOI reflects its strongest scores on all four sociocultural factors (corruption, political risk, education and regulatory environment). Serbia's low ranking reflects its lowest scores on all factors except education, and especially for its higher political risk. Its score is lowest of all countries, including Russia. Scores for all countries except Serbia are closer to Turkey (49) and Greece (43) and are well above Russia (38). They are still separated from their lowest scoring western neighbor Italy by a minimum of 21 points.

The five Balkan countries examined clearly have accounting values that indicate an opportunity to focus on areas that may need to be strengthened for successful implementation of IFRS in many companies, and in the practice of local accountants and auditors. They face the same cultural challenges as their Balkan neighbors, but their scores indicate that they are, with the exception of Serbia, stronger in IFRS cultural orientation than Russia. In all basic areas including corruption, there is some room for improvement in comparison with Italy, Austria and the United States. The key to improvement is to identify potential weaker areas based on socio-cultural analysis and to utilize available educational and professional training resources from the IASB, Big Four Accounting organizations and other organizations to improve the orientation of local company accountants, auditors, and those studying to enter the profession. Russia, with its relatively low index scores, has been effective in pursuing these solutions. (Borker, 2012a)

CONCLUSION

In the case of the Balkan states, the IFRS indices provide a more objective basis for characterization of each country's IFRS orientation, as compared with an earlier study of Central and East European accounting culture and IFRS (Borker, 2012c). The data suggests IFRS orientation comparable to Turkey and Greece and well below Western European EU members. Emphasis should be placed on providing high level professional training to students and existing accountants with strong emphasis on professionalism and high ethical standards.

This study supports the value of quantifying Gray accounting value dimensions to study and compare individual countries, and, for qualitative judgments about the closeness of individual country profiles to an IFRS favorable profile. Scores obtained using the Composite IFRS Orientation Index and the Expanded IFRS Orientation Index provide useful cultural information which opens up the opportunity to seek and apply educational, training and institutional solutions to improve the development of an accounting culture that will support IFRS. Even where other factors have caused countries like Russia, with a relatively low index score for IFRS orientation, to move forward with the adoption and implementation of IFRS, the indices' diagnostic tools can do much to ensure that accounting professionals and trainees are capable of meeting these tasks. While large companies can rely heavily on the Big Four and other international firms to assist them with IFRS implementation, there must be a strong effort made to allow information to penetrate the masses of accountants, auditors and bookkeepers at the more local level.

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