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# Three Audit firms and their implementation and knowledge transfer of IFRS

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# Summary

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**Five key words:** IFRS, audit firms, knowledge, knowledge transfer, interpretation

**Purpose:** The purpose of this thesis is to identify similarities and differences in implementation and application of IFRS in the Big Four audit firms. In order to do this we are going to see how interpretations of IFRS are shared and transferred within the audit firms.

**Methodology:** We have chosen to use a case study approach with a qualitative approach and an abductive view. When collecting the data we have chosen to use interviews, literature and documents from audit firms.

**Theoretical perspectives:** Prior research of knowledge, knowledge intensive companies, knowledge transfer as well as research regarding IFRS.

**Empirical foundation:** Case study approach; three in-depth interviews with employees of Deloitte, Ernst & Young and PricewaterhouseCoopers, homepages and documents from the three audit firms.

**Conclusion:** The study shows that there are more similarities than differences in channels and strategies that the Big Four audit firms use when interpreting and implementing IFRS. We found that codified knowledge plays a huge part when the audit firms transfer and share information and knowledge, especially the extensive use of databases was evident. However, the interpretations made by both the respective audit firms and the employees can differ which derives from the use of a principles based accounting system and because individuals patterns of life affects how an employee perceives their reality.

# Vocabulary

EU	European Union
FAR SRS	Föreningen Auktoriserade Revisorer (FAR) Svenska Revisorsamfundet (SRS)
FASB	Financial Accounting Standards Board
GPPS	Global Public Policy Symposium
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
IFAC	International Federation of Accountants
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standards
IASCF	International Accounting Standards Committee Foundation
SAC	Standards Advisory Council
SEC	United States Securities Exchange Commission
US GAAP	United States Generally Accepted Accounting Principles

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# 1 Introduction

## 1.1 Background

As companies become more international, globalization is affecting the business world in an increasing pace and more companies are operating across borders. This has created a more regulatory environment that affects the audit profession and it has become necessary for both companies and audit firms to keep up with the new environment. New regulations such as the EU regulation (1606/2002) from 2002 and the Sarbanes Oxley Act of 2002 as well as the New 8<sup>th</sup> Company Law Directive from 2006, has affected the audit profession (Vera-Muñoz, Ho & Chow, 2006).

Today, there are four audit firms dominating the market; Deloitte Touche Tohmatsu, Ernst & Young, KPMG and PricewaterhouseCoopers, also known to the public as the Big Four. In 2006, 94 % of audit fees paid by public companies were gained by the Big Four audit firms (GAO Report, January 2008). These large audit firms have immensely grown in both size and importance and each operate in over 140 countries (Annual Review from 2008 reports of Deloitte, Ernst & Young, KPMG, PricewaterhouseCoopers). This have made the largest audit firms important governance bodies as they for example reach more jurisdictions than the International Federation of Accountants (IFAC), who cover 122 countries and jurisdictions (IFAC homepage: About IFAC). The Big Four audit firms therefore have a huge impact on listed companies today as it is up to these audit firms to approve a company's consolidated financial statements (Loft, Humphrey & Turley, 2006).

## 1.2 Discussion of problem

The International Accounting Standards Board (IASB) issue International Financial Reporting Standards (IFRS) which are intended to achieve convergence in accounting as a way to eliminate differences in national approaches however, many challenges remain (Tokar, 2005). The International Accounting Standards Committee Foundation (IASCF) set up the International Federation of Reporting Interpretations Committee (IFRIC) in 2002 as an interpretive body of the IASB. However, the output of IFRIC during the years 2002-2007 was only 14 Final Interpretations (Bradbury, 2007). The low outcome may result in that the interpretations of standards will in reality be made by other organizations than IFRIC. Both companies and audit firms need to make day to day decisions on implementation and guidance difficulties, thus developing their own interpretation as a supplement to those interpretations issued by IFRIC (Tokar, 2005).

The audit firms' interpretations need to be shared within the audit firms to achieve a consistent application. This is important since a knowledge intensive company, such as an audit firm, rely heavily on each individual as the embedded knowledge of each individual employee is seen as a vital resource (Alvesson, 2000 in Finnback, Gunnarsson, Johansson & Silfver, 2008). A successful firm is built by its reputation and the education of the provider as the consumer usually lacks the ability to evaluate the quality of the outcome (Gstraunthaler & Kaml, 2007). Therefore, the success of the firms is determined by the employees experience and knowledge.

Implementing and applying IFRS is an important part of audit firms. As the IASB publishes new standards and guidance, each of the published information needs to be interpreted, implemented and applied accordingly by the audit firms and this knowledge needs to be transferred within the firm. If the implementation processes of IFRS in the audit firms are not successful, the knowledge of the standards will not be transferred to the employees and the standards will be interpreted differently.



There are various factors affecting the implementation and application of standards and guidance published by the IASB. All of the Big Four audit firms function on a global basis, with each member firm within the global organization reporting their independence as separate legal firms to limit the legal liability (official websites of Deloitte, Ernst & Young, KPMG, PricewaterhouseCoopers), which is a result from the Anderson collapse in 2002. Operating in many jurisdictions the Big Four audit firms are struggling to avoid differences by achieving a common and single view on specific issues while remaining independent legal firms (Tokar, 2005).

This brings us to the focus of this thesis. An increasing concern has arisen that each users' interpretation of the published information by IASB may differ, thus creating a variety of approaches and interpretations. With a globally accepted focus on convergence (IASB, FASB, EU etc.), the interpretations of standards becomes an important ground stone. The interpretations and applications, i.e. the knowledge, need to be transferred within the audit firms to get a consistent application of IFRS. The Big Four audit firms have the majority share of the market when referring to the auditing of listed companies (GAO report, January 2008). Therefore, their interpretation will greatly affect the application of IFRS.

The authors are interested in the differences and similarities in how the Big Four audit firms implement and then apply these standards internally, and how the interpretations are shared within the firm. When each audit firm creates its own interpretations, the risk of different interpretations may increase. Also, how the audit firms are able to transfer this knowledge throughout their member firms which might give an idea of how they want the interpretation to be made.

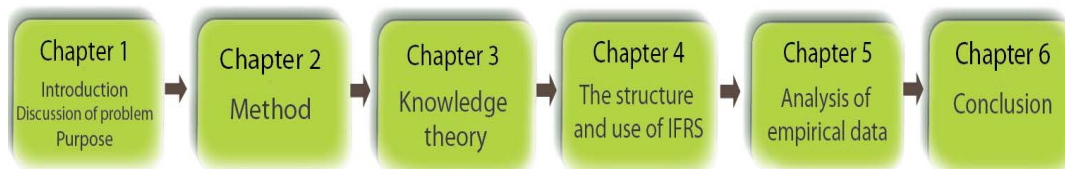
This comes down to our main research question:

“How do audit firms implement and apply IFRS, and how does the audit firm transfer this knowledge throughout their organization?”

## 1.3 Purpose of the research

The purpose of this thesis is to identify similarities and differences in implementation and application of IFRS in the Big Four audit firms. In order to do this we are going to see how interpretations of IFRS are shared and transferred within the audit firms.

## 1.4 Disposition



*Figure 1: Disposition guide*

In **chapter one**, we introduce the subject matter and discuss the problems with the implementation and knowledge transfer of IFRS. Also, our main research question is presented and our purpose of the research.

In **chapter two** we present our methodological considerations. Our choice of knowledge view, our research approach, what kind of methods we used to collect the empirical data and discussions regarding our choice of methods will be illustrated in this chapter.

In **chapter three** we set out our theoretical framework and relevant theories will be presented and explained. Chapters three and four are the base for the analysis later in the thesis. We give a presentation of knowledge theories and the different forms that knowledge can take.

In **chapter four** we will describe the accounting system, structure and the use of IFRS. The chapter also includes a presentation of Tokar's article regarding KPMG

and Bäckström's article describing the handling of an IFRS issue in Sweden as well as explaining IFRIC's role as the interpretative body of IASB.

In **chapter five** we first introduce the three audit firms. We will then intertwine the empirical data with the theories previously presented which results in an analysis which is going to answer our main research question.

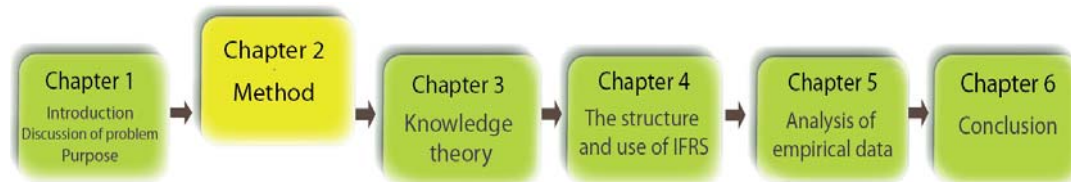
In **chapter six**, which is the last chapter of this thesis, we summarize our findings and the chapter ends with a few words regarding continued research.

# 2 Methodological considerations

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In this chapter we will present our choice of methods and approaches. We will discuss the different methodological considerations to give the reader an understanding of the thesis and its structure.

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*Figure 2: Disposition guide*

In our thesis our choice of method is a qualitative approach as the purpose is to understand how audit firms create and transfer knowledge to be able to implement knowledge of IFRS within the audit firm. When collecting the data we have chosen to use interviews, literature and documents from the audit firms. We have interviewed employees of three audit firms: Deloitte Touche Tohmatsu, PricewaterhouseCoopers and Ernst & Young. We are going to have an abductive view to solicit theory and empirics to identify and distinguish whether the theory and empirics connects with each other.

## 2.1 Qualitative method

We have chosen to use a qualitative method because it is most suitable to our main research question. To answer our main research question, we have chosen a method that graduate and that often requires few concentrated units. This kind of method is suitable for qualitative data collection (Jacobsen, 2002). Also, by using the qualitative approach we are going to select information through interviews.

By using the qualitative perspective, you watch the surrounding reality subjectively and this means that the reality is an individual, social and cultural construction. When researching the interest is to study how individuals perceive and interpret the reality. In the qualitative perspective the researcher finds theories and derives and examines the hypotheses to verify it, which we aim to. The qualitative method is also not standardized; instead it is flexible and gives a lot of space for variations (Backman, 2008). Possible effects when using qualitative methods when doing interviews are that the researchers have to be aware of the interviewer effect and context effect. The interviewer effect is when the interviewers' presence can create certain results, for example the respondent can answer in a certain way because the respondents believe that the interviewers reward certain answers (Jacobsen, 2002 and Svenning, 2003). The context effect is when the location of the interview can affect the results (Jacobsen, 2002).

The interviewer effect will not have an impact on our results because the respondents, according to us, have not answered the questions in a certain way under our influence. The context effect is not a problem due to our interviews took place at the respondents' respective office and we suppose that the respondents are comfortable in their office and thereby can talk more freely. We consider that our research has a high reliability due to if our research is going to be reproduced the result from our empirical data is going to have the same result when a new researcher asks the same interview questions again (Bryman & Bell, 2003).

According to Backman (2008) a common misunderstanding with qualitative method is that it is easy to carry out however, observations and interviews demand a lot from the researchers for example compiling surveys. In the qualitative perspective the respondents is chosen via other criteria than through statistic criteria to obtain an increased understanding of the respondents and of the research. These criteria for choosing respondents can be changed during the research period to get a better understanding of the research question. Another problem with the qualitative view is if a respondent do not answer the interview questions correct and honestly. The flexibility is an additional problem concerning that new information constantly arises (Jacobsen, 2002).

We are aware of the disadvantages with qualitative approach concerning the time and effort. When choosing the respondents we contacted the three audit firms and asked whether we could do interviews regarding IFRS. Each of the three audit firms then chose a respondent that they thought could answer our questions. We do not see a problem with not being able to select our respondents. The audit firms know better than we do which employees are suitable to ask questions about IFRS to.

A disadvantage with qualitative approach is that it only reaches few individuals which can create a problem with the representativeness in the group the respondent represent and this is a common generalization problem along with the external validity. Also, the amount of data the qualitative approach offer can become a problem if the researchers are open for more information, and there is a risk that the researcher strains the information (Jacobsen, 2002).

Our choice of only taking three of the Big Four audit firms into consideration and drawing a general conclusion regarding all of the Big Four firms can lead to us missing out information about the other firm which could affect our result. The motive why we do not have KPMG as our case company in our thesis is for the reason that we did not get an interview with KPMG.

On the other side, due to the fact that we used three of the Big Four audit firms, we can draw better conclusions whether their interpretation and knowledge transfer of IFRS differ between the Big Four audit firms and also see the result in a context, compared to if we only had two of the Big Four audit firms.

However, by taking articles into consideration, one from Mary Tokar (2005) describing KPMG and their problems when converging and implementing global standards and another article from Anders Bäckström (2009) about challenges when applying IFRS, we hope to get a broader picture about the Big Four audit firms' situations when implementing and transferring knowledge. As both of these articles are secondary sources and since we do not have the time to control if the information given in these two articles are correct, we assume that the information are reliable and truthful. Though, the journal that Bäckström's article is published in, is an established journal and thus according to us a trustful source and the fact

that he is an authorized auditor in Sweden, we consider his article reliable. Another aspect that has to be taken into consideration is the fact that Bäckström is not a researcher in the sense that he does not perform a research at a university with academically methods which can result in the article being less reliable. Tokar is a partner at KMPG LLP (US) and a member of IFRIC, the IASB's interpretive body. The fact that she is not a professional researcher has to be taken into consideration however, her deep engagement in interpretation and application matters will give us an important aspect in this thesis.

We are also aware of the fact that IFRS and the interpretations from the audit firms are changing from year to year and new information constantly arises which could lead to that the result of this research can be invalid when the environment and the standards of IFRS change.

## **2.2 Research approach**

We have chosen an abductive reasoning approach. Abduction has some features from both inductive and deductive method but under the abductive method the empirical application area and theories develops, adjusts and refines. The abduction is based on empirical facts just as the inductive method, however the abductive theory is closer to the deductive method because it does not reject theoretical ideas as the inductive method does (Alvesson & Sköldberg, 1994, 2008). According to Alvesson and Sköldberg (2008) the abductive method has some similarities with the hermeneutic approach and it is also often used when doing case studies (Alvesson & Sköldberg, 1994). When using the abductive approach, the research process is alternated with theory and empirics which is interpreted from each other (Alvesson & Sköldberg, 2008).

The reason why we chose the abductive approach is that we intend to collect the empirical data by interviews to study how the audit firms implement and transfer knowledge within the audit firm but before we collect the empirical data we aim to acquire theoretical starting points. After collecting the empirical data, we aspire

to compare theory with the empirical data to see if it corroborates. The interviews can lead to several different answers and conclusions and therefore we have to adjust the theory with the empirics or adjust our purpose during our research. When doing this the research will get a better stream and the reader can easier follow the flow of our paper.

## **2.3 Case studies**

In general, case studies are used when the researchers have chosen a qualitative interview method and case studies have sometimes been compared with qualitative research because a case study is built on qualitative data (Lundahl & Skärvad, 1999). According to Backman (2008) case studies are often used when to examine, understand, and explain organizations or systems and a case study can be either explorative or descriptive. Jacobsen (2002) adds that a case study should be used when the researcher wants a deeper understanding of a certain case.

Svenning (2003) adds that a case study consists of more than one source of data and the researchers choose one or more companies or other objects to study, and the most suitable data collection methods. The fact that KPMG is not included in this study is not a problem since we have chosen to do a case study approach. In a case study, as mentioned above, the researchers only study few objects. We are going to, just as Svenning explains, use interviews, literature, documents from the audit firms and other sources for our data collection when we study the three audit firms. Our choice of data collection methods will be described below.

### **2.3.1 Interviews**

We have chosen to use interviews as one of our main methods for data collection. The motive why we chose interviews is due to the information we wanted is more related to the process when transferring knowledge and to acquire this information we had to ask the audit firms because that information is not accessible on the



audit firms' homepages or in their annual reviews. It is important to examine the formation of interviews that will be used, who should be interviewed which interview technique to use and how the interview data should be compiled and analyzed (Lundahl & Skärvad, 1999). These criteria will be described below.

### **2.3.1.1 Formation of the interview**

When we performed the interviews we used a semi-standardized structure which means that we in advance had prepared a couple of questions with some follow-up questions. The less standardized the interview is, the more the answers get gradate and comprehensive (Lundahl & Skärvad, 1999). The reason for the semi-standardized interview is that sometimes the respondent gives a short answer, the respondent does not answer the question or we need a deeper answer in a specific question.

We also used an unstructured interview where the respondent formulated the answer by him or herself i.e. we did not give any answering alternatives (Lundahl & Skärvad, 1999). We chose to divide the interview into two parts where the first part deals with personnel background and employment and the second part handles IFRS. Some questions in our interview guide were closed, i.e. not discussion questions, because we wanted to compare the answers between the respondents. Other questions were left open for the respondent to discuss due to that we wanted to know as much as possible about their implementation and knowledge transfer of IFRS.

We did not perform the interviews in English for the reason that the respondents' native language is Swedish and we assume that the respondents are more comfortable answering the questions in Swedish rather than in English. Also, the respondents can better formulate the answers and express what they mean more easily in Swedish. The interview guide is also in Swedish (Appendix A) but we have translated the guide into English (Appendix B) and we reserve for possible translation formulations.

When we decided to do interviews in respective audit firm, our aim was to do interviews where the two of us were present and could ask the questions to the respondent directly. However, it was only at one firm, Deloitte, where we performed the interviews at their office. The interview with PricewaterhouseCoopers was performed via a telephone interview because the respondent is located at their office in Stockholm and we did not have the time to travel to Stockholm. The third interview with Ernst & Young also differed from the other interviews due to that they were uncertain if the information they would give us was confidential and therefore the interview was performed via e-mail. This should be taken into consideration because, just as Ernst & Young mentioned, a disadvantage of this kind of interview is that we cannot do interpretations and spontaneous questions of the respondents' answers. On the other hand, an advantage with this interview is that the respondent will consult with the people responsible for IFRS in Ernst & Young in Sweden when answering our questions. We want to underline that the respondents answered the same questions i.e. we sent the interview guide in advance to all of the respondents which made it easier when we performed the interviews by phone and via e-mail.

The interviews with Deloitte and PricewaterhouseCoopers do not, according to us, differ in result because in both cases we could ask follow up questions if we wanted certain or deeper answers and we do not take their body language or certain doubts into consideration, we just analyzed the answers they gave us. As an outcome the third interview with Ernst & Young did not either differ in result, except for dissolute answers from the respondent and the lack of follow up questions which we resolved through sending e-mail with follow up questions. Nevertheless, this should be taken into consideration.

### **2.3.1.2 The respondents of the interviews**

When we decided to perform interviews we contacted the three audit firms and the contact person in respective audit firm then chose an appropriate interview person. We had in advance announced what kind of respondent we wanted to

interview. We decided not to select the respondents ourselves because the three audit firms; Deloitte, PricewaterhouseCoopers and Ernst & Young, are the biggest audit firms with over thousands of employees in Sweden and we did not have the time to select and bone up their organizations to be able to choose an appropriate respondent. However, the selection method of the respondents should be taken into consideration.

One respondent is a female partner at Deloitte. She works, if not daily but often, with IFRS and listed companies in Malmö, Sweden. Our second respondent is a male at PricewaterhouseCoopers in Stockholm whose title is accounting specialist and he works daily with questions regarding IFRS. The third respondent is also a female and works at Ernst & Young in Malmö, Sweden. She is a senior manager at Ernst & Young and works often with IFRS questions. We have not taken the gender perspective into consideration in the selection of respondents because we do not consider that as a factor which will affect the result of our research.

We have only conducted three interviews, one with each audit firm. We are aware of that three interviews might limit our empirical data. Unfortunately, we were only given these respondents. The results should not vary if we had interviewed more respondents at respective audit firm because we did not want their personal opinions but rather how the organization functions. The respondents met our requirements as they have worked at respective audit firm for 10-20 years and as described before, everyone is well acquainted with both IFRS and its standards and their respective organization.

### **2.3.1.3 Interview guide**

We used a digital Dictaphone in two of the interviews to be able to transcribe the interviews afterwards and to easier compare the answers. The digital Dictaphone gives an advantage when interviewing to remember the exact wording or tone and when referring back to the interview.

In all of the three interviews, the same interview guide was used. The interview guide is divided into two parts. The first part take care of personal background

and employment and questions such as how long the respondent have been employed at the audit firm, the title of the respondent, the respondents main job assignment and a question about knowledge transfer. The second part of the interview guide deals with IFRS and questions for instance if the audit firm have a central interpretation unit of IFRS, who interprets IFRS at their audit firm, how do the standards and interpretations transmit at their audit firm, what support do an auditor get in IFRS at their audit firm, if there are IFRS experts in every office, if it is easy for an employee to find information about IFRS at their firm, how an auditor handles uncertainties and interpretation difficulties of IFRS, what kind of quality controls the audit firm has, what standard is most problematic and if there are any differences in the interpretation of IFRS between the audit firms.

Our purpose with the interview guide was to find certain processes regarding IFRS. The questions in our interview guide has been answered and the questions match our purpose, empirical data and our theoretical framework which gives our research study a high degree of validity (Bryman & Bell, 2003).

#### **2.3.1.4 Procedure**

The first thing we did was to contact the audit firms and presented our discussion of problem and the purpose of our thesis. At respective audit firm we got a contact person who chose suitable respondents that we could interview. Then we decided together with the contact person how to conduct the interview and which date the interview should take place. The interview with Deloitte took place at their office in a quiet meeting room. In the interview with PricewaterhouseCoopers, the respondent was at his office and we had a speakerphone to record with the Dictaphone. At the two interviews described, there were no distractions during the interview. In both interviews we had one interview leader who asked the questions and the other one asked eventual follow up questions. Also we informed the respondents that we taped the interviews and that we would send eventual quotes to them before we send in our thesis. In the Ernst & Young interview we first sent our interview guide, they sent us the answers via e-mail and we then sent back eventual follow up questions.

After the interviews we transcribed the answers and read through the interviews once again. Since we have an abductive approach we analyzed and altered the empirics and the theoretical framework with the transcribed material and came up with an analysis and a conclusion.

### **2.3.2 The search for literature**

When searching for literature our aim was to find facts about knowledge and IFRS. Since the authors of this thesis wrote about knowledge and the different shapes that knowledge can take in their candidate thesis, we have referred to our thesis from 2008. We have used more of the basic facts from the thesis from 2008 and added new and deeper facts about knowledge in this thesis. Before collecting the empirical data, we searched for literature that had found differences in IFRS interpretations, as well as how the audit firm uses and applies IFRS. After collecting the empirics, we found more literature about knowledge but with emphasis on implementations of IFRS. The reason for this is that we wanted to strengthen our empirics.

To summarize, we have searched for two kinds of literature, both literature regarding IFRS and literature concerning knowledge and knowledge transfer. We have used the University of Lund's libraries' databases as a starting point because we found it to be a suitable source when retrieving academically articles and books. Our key words when searching for the literature were mostly focused on: knowledge, transfer of knowledge, audit firm, IFRS, implementation, interpretation and Big Four audit firms.

### **2.3.3 Documents from the audit firms**

The main documents that we have taken into consideration from the audit firms are the three audit firms' annual reviews. We have tried to use the recent annual reviews to utilize more updated materials. The annual reviews that we have used

are the Swedish member firms' annual reviews and the global firms' annual reviews. We have also used the audit firms' homepages to retrieve more documents from the audit firms such as newsletters, organizational structure and other documents. We are aware of that the documents from the audit firms are biased and most of the documents are selling in the sense that they are addressing their customers. We have tried to use as little biased information as possible in this thesis and we have only used the documents in an information purpose. Some information from the audit firms is difficult to obtain due to the competition aspect between the Big Four audit firms.

## **2.4 Primary and secondary data**

Data can be divided into two different kinds of data, primary and secondary data, which are also called firsthand respective secondary sources. The firsthand source is directly from the "source" and a firsthand source is a person who has been involved in or has observed events or conditions. In our research we have used both primary and secondary data. Interviews are mostly a primary data source (Svenning, 2003) however, some answers could also be secondary data because the interview person may not be involved in the process itself.

To summarize, one source of primary data used in this thesis was interviews. We have also used the audit firms' homepages where we found various forms of documents although we are aware of that the material is biased. We consider this material as primary data in this thesis due to our research question.

The literature and the two articles by Tokar (2005) and Bäckström (2009) used in this thesis is to be considered as secondary data as well as the use of our candidate thesis from 2008.

# 3 Knowledge theory

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Chapter three is the first of two chapters in which we will present our theoretical framework. In this chapter we will lay forward our theoretical framework by presenting theories regarding knowledge and the different forms knowledge can take.

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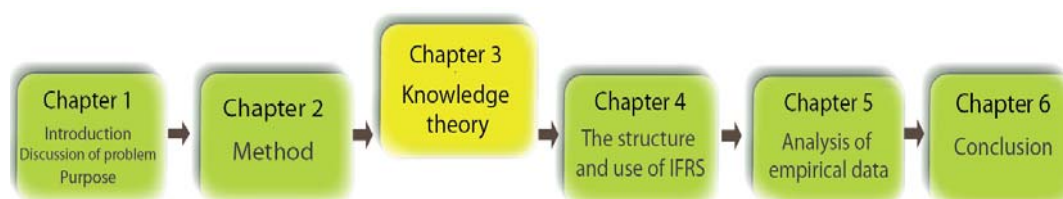


Figure 3: Disposition guide

## 3.1 Definitions of knowledge

The purpose of this thesis is to study differences in how the audit firms' interpretations are implemented, shared and transferred within the audit firm. Therefore, it is important to describe and understand knowledge to recognize the context and the content in this thesis. However, knowledge can be defined in different ways and there does not exist any specific definition that researchers have agreed upon (Finnbäck et al, 2008). Sveiby (1995, as referred to in Finnbäck et al, 2008) believes that there exist two definitions of knowledge, the first one is characterized by *to know* which means to have ability and the other one is described by *to know something*. By ones actions, according to Sveiby, an individual can prove that the person can do what it says in practice. This action would imply that an individual either knows something or it does not.

An another definition of knowledge illustrated by Finnbäck et al (2008) is from Hislop (2005), where knowledge can be seen through a hierarchical perspective and Hislop (2005) distinguishes between data, information and knowledge. According to this definition, information should be seen in a context with an

understanding of how the specific information should be used. This view of knowledge is also shared by Shultz (2001, pursuant to Finnback et al, 2008) and Rooney (2003). Rooney defines the term data as unorganized bits that makes for building blocks of information and views data as relatively uncolored by human cognition, emotion or consciousness. When data gets organized in any form of text or statistics it is transformed into information and is usually transmitted through books or via Internet. Knowledge is constructed in the process of making sense of information. However, more and more information does not necessarily lead to knowledge as it may become *noise* instead. According to Rooney (2003) knowledge is made up by more than facts. It is colored by individuals' beliefs and values.

Finnback et al (2008) continues to define knowledge by taking Wikström's and Norrman's (1999) definition of knowledge into consideration. According to them, knowledge is divided into four parts; information, know-how, explanation and understanding. Information is objective information; know-how is information tied to the individual and the individual should be able to use the information in practice; explanation is described as causation and helps to solve problems through scientific articles, textbooks and encyclopedias; and understanding occurs when the individual can understand principles and contexts which are connected to the individual.

Sallis and Jones (2002) list the characteristics of knowledge as: more than information, it is social, it is a key organizational asset, knowledge is constructed in the mind of a knowing subject, it is active understanding, it depends on an individual's perspective, it is an integral element in learning and knowledge is both explicit and implicit.

### **3.1.1 Explicit and implicit knowledge**

A common viewpoint is that knowledge can be divided into two types of knowledge; explicit and implicit knowledge (Sallis & Jones, 2002). It is important to understand the differences between explicit and implicit knowledge to



comprehend the various existing definitions of knowledge. However, within organizational theories there is no consensus among researchers whether it is possible to divide implicit and explicit knowledge (Finnbäck et al, 2008).

Implicit knowledge has been used as a synonym to the term tacit knowledge. Both implicit and tacit knowledge are defined as a more informal and private knowledge, to some also seen as unconscious knowledge. Many have elaborated on Polanyi's work of 1966, *The Tacit Dimension* (Sallis & Jones, 2002).

Unarticulated, non-verbalized or non-verbalizable knowledge is called tacit knowledge. The contrast of tacit knowledge is explicit knowledge. Explicit knowledge is highly codified, articulated knowledge which can be transferred in systematic language (Evangelista & Hau, 2009). Polanyi's term tacit knowledge has had great impact on the knowledge management field. His definition of tacit knowledge can most easily be explained through his more common usage of tacit knowing (Day, 2005). Tacit knowledge highlights knowledge as deeply rooted in the experiences and values and culture of an individual, relating to the subjective dimension of knowledge (Sallis & Jones, 2002).

Nonaka and Takeuchi have done most work in linking tacit knowledge into the managerial theory (Sallis & Jones, 2002). According to Finnbäck et al (2008) who refer to Nonaka (1991), explicit knowledge is pronounced and codified knowledge while implicit knowledge is knowledge that is implicitly as in tacit knowledge. Tacit knowledge is defined as when an individual knows how to perform a task without the ability to explain its action in words, and thus implicit knowledge depends on the individual's eloquence and the spread of knowledge is going to be irregular since the degree of eloquence differs between individuals (Finnbäck et al, 2008 referring to: Realin, 1998; Pleasants, 1996; Kalling & Sthyre, 2003). This is in line with the work of Polanyi, who claims that people know much more than what they can tell, thereby insinuating that tacit knowledge is difficult to communicate and thus also difficult to share (Sallis & Jones, 2002). According to Sveiby (1995, referred to in Finnbäck et al, 2008) an individual builds up a pattern of behavior during its lifetime and these patterns work as unconscious actions. It is important to note that the information one individual

extends to another is not the same information that another individual accepts and creates. With this reasoning in mind, Sveiby (1995) implies that implicit knowledge differ between individuals and a recipient have to try, practice and reflect the information when knowledge is transferred to him or her. However, each individual have limitations because the knowledge an individual possesses depends on the knowledge the individual already has (Sveiby, 1995).

Finnbäck et al (2008) proceed with another interpretation of knowledge from Takeuchi and Nonaka (1995) who argues that explicit and implicit knowledge cannot be separated since knowledge is not verifiable and measurable. However, knowledge can be pictured as an iceberg with explicit knowledge illustrated as the top of an iceberg above water and implicit knowledge the part still under water. As Malone (2002) points out:

*“Unfortunately, the truth that Polanyi (1966, p4) alludes to is that there will always be more knowledge known than documented”* (Malone, 2002).

Trough the various definitions, descriptions and explanations above we have attempted to define knowledge. A conclusion that could be drawn is that many researchers have all tried to explain knowledge but cannot agree upon one general explanation. We believe and will in this thesis use the above reasoning as a base of theory. As in Finnbäck et al (2008), we assume that the different types of knowledge are hard to separate, especially explicit and implicit knowledge, because both of them impregnate an individual’s knowledge. It is instead the different dimensions of explicit and implicit knowledge that reflects the knowledge within individuals in addition to an individual’s subjective dimension of knowledge.

## **3.2 Knowledge intensive company**

According to Finnbäck et al (2008) a knowledge intensive company is defined as a company whose assets consist of the employees’ special knowledge and skills. Another definition is provided by Alvesson (2004), from Finnbäck et al (2008),

who mean that a knowledge intensive company is an organization whose value comes from the use of advanced knowledge and whose main competitiveness is an effective method to use the intellectual capital. Alvesson (2004) continues to describe a knowledge intensive company by analyzing its characteristics. A knowledge intensive company uses more problem solving and non-standardized production compared to labor intensive and capital intensive companies.

The employees in knowledge intensive companies often have a high level of education and the employees requires to be able to work independently and creatively (Finnbäck et al, 2008). A knowledge intensive company is vulnerable because the company's most critical elements are the employees, networks, customer relationship, manuals and service provider systems (Finnbäck et al, 2008 from Alvesson, 2000). In general, all companies have an enormous amount of information and knowledge tied to the organization. If the information and knowledge is used effectively it can be turned into a comparative advantage. This is where a company might encounter complications as the utilization of knowledge is not an easy matter (Sallis & Jones, 2002).

Vera-Muñoz et al (2006) define audit firms as knowledge intensive companies based on how the client engagement include teams where each individual need to perform to succeed. The knowledge and expertise need to be shared among the audit firms' members as this may impact how the audit will be conducted as well as the outcome. According to Vera-Muñoz et al (2006), the quality and efficiency of the audit firm depends on the power to act effectively when trading skills, knowledge and best practices so members can be able to reuse the information given and in the same time minimize information overload.

Another characteristic of a knowledge intensive company is that the organizational hierarchy is toned down as well as a high degree of independence (Alvesson, 2004 referred to in Finnbäck et al, 2008). Ekstedt and Jönsson (2001, in Finnbäck et al, 2008) points out that flat, decentralized organizations gives the employees the liberty and freedom which leads to more opportunities to develop than in centralized organizations. According to Ekstedt and Jönsson (2001) decentralized information and knowledge exchange benefits from flat

organizations, the boundaries within the company will become more unclear which will result in information and knowledge flowing in every direction (Finnbäck et al, 2008).

### **3.3 Transfer of knowledge**

Scholars have described globalization as a 'postindustrial era', as the 'information age' or as a 'knowledge society'. This is a phenomenon deriving from the departure from the previous domination of manual labor in the West as a result of the increased importance of innovations and information and communication technologies. All companies depend on the capacity to transfer and manage knowledge in the most effective way (Nicolini, Gherardi & Yanow, 2003).

The awareness of transferring knowledge has lately increased in organizations and corporations (Hansen, Nohria & Tierney, 1999 in Finnbäck et al, 2008) and many studies have been made to identify the most effective way of transferring knowledge. The least effective way to transfer knowledge was found to be through listening to lectures where listeners after five days remember less than 10 % of the received information. However, through hearing and listening a person remember just about 20 % as a contrary to if the individual instead perform something in practice an individual remember up to 60-70 % (Sveiby, 1995 in Finnbäck et al, 2008).

Vera-Muñoz et al (2006) claim that if an audit firm does not support effective ways to gather, sort, transform, record and share knowledge imbedded within the employees' knowledge as a valuable resource will be wasted.

To be able to observe how audit firms interpret IFRS (creating knowledge) and spread this information within the firm (the transferring and sharing of knowledge), and how the employees use the information given (how they learn), it is important to give a wide scope to the terms used later in the thesis. There are different theories relating to the wide spectrum of knowledge. We are going to concentrate on two of these: knowledge management and organizational learning.

## **3.4 Knowledge management**


Knowledge has entered the center stage in various disciplines, from sociology to economics and management science (Davenport, De Long & Beers, 1998). Distinguishing between what knowledge and information is can be troublesome. As companies see knowledge more as an asset, companies attempt to explore effective ways to create, share and use knowledge. It seems safe to say, knowledge management has blossomed.

### **3.4.1 Definitions of knowledge management**

Within the area of knowledge management, researchers try to identify how an organization can identify, create and receive knowledge to be able to use it and according to Braf (2000) knowledge management can be divided into two different perspectives: information management tool and strategic tool (Finnbäck et al, 2008). The information management tool is to collect and store the individuals' knowledge and the knowledge is then meant to reach other employees within the company. The strategic tool focuses on knowledge sharing in an effective and accessible way, and gives the right presumptions for knowledge transfer through good communication, how the company's culture is expressed and the reward system (Finnbäck et al, 2008). Nonaka and Takeuchi (1995) describe an additional definition of knowledge management and defining knowledge management as a company's capacity to create, spread and embodiment the knowledge in its products and services (Finnbäck et al, 2008).

#### **3.4.1.1 Factors effecting knowledge management**

Davenport et al (1998) identified eight major factors that affect the effectiveness of knowledge. The factors that are relevant to this study have been taken into consideration.

-  The technical and organizational infrastructure

A broader infrastructure will facilitate the finding and usage of relevant knowledge.

#### ✚ Standard and flexible knowledge structure

This basically means that a database with a total lack of structure will make the retrieval of knowledge difficult. When creating a database the systems infrastructure requires clear categories and key words.

#### ✚ Knowledge friendly culture

The knowledge management system should fit the organizational culture and a positive attitude from employees towards both the creation and sharing knowledge within the firm is important.

#### ✚ Multiple channels for knowledge transfer

Information and knowledge is today shared through multiple channels contributing to the effectiveness of knowledge transferring. The Internet and other global communication systems help a company to decrease the need for people to people communication. One channel does not diminish the need for another, they rather reinforce the other.

#### ✚ Senior management support

The need for having a senior management that supports the knowledge management system within the company was evident in Davenport et al's (1998) study.

No factor is more important than another, rather the factors are seen as related, but with the support of knowledge oriented culture from the management is still seen as a major influence of the success of the knowledge management system.

To continue on Davenport et al's (1998) factor of *Standard and flexible knowledge structure*, Furner, Mason, Mehta, Munyon, & Zinko (2009) have studied to what correlation learning preferences are connected with culture in a knowledge management system (KMS). KMS is computerized information in which an organization can capture and store embedded knowledge, both from

employees and from their customers. As companies rely deeply on information and knowledge to be transferred and shared within the organization the outcome of learning will depend on how the KMS is designed. Culture according to the authors is defined as:

*“Patterns of values, beliefs, norms and customs shared by members of a civilization that influence their behaviour.”* (Furner et al, 2009).

Furner et al’s (2009) study resulted in culture affecting the effectiveness of learning outcome. The national culture embedded in the employee seemed to impact learning outcomes and thus supporting the researchers’ hypothesis.

### **3.4.2 Knowledge management within audit firms**

King, Chung and Haney (2008) have created a lifecycle over knowledge management to easier see how the information and knowledge flows within the company. We are interested in both the creation and acquisition part where each audit firm decides on which materials to use, and how this knowledge is transferred and shared within the organization. Knowledge creation refers to Nonaka’s four models of knowledge creation, which are: socialization, externalization, combination and internalization. Knowledge acquisition is connected to the search, recognition and assimilation of knowledge that might be of value to the company and this knowledge is usually found outside of the company (King et al, 2008). The information or knowledge has then to be *transferred* or *shared* in the company. To *transfer* information or knowledge is a focused and deliberate communication from the sender to the receiver whereas to *share* information is a seen as a less focused communication of knowledge, for example through the company’s knowledge database (Finnbäck et al, 2008).

Ribiere (2009) emphasizes the importance of organization culture as a part of knowledge management. He states that even with the best incentives and tools available for transferring and sharing knowledge it would not give the company

advantages if the organizational culture and employees remain reluctant to share or acquire knowledge.

According to Ribiere (2009) two different knowledge management approaches has surfaced. One is the codification approach, where IT plays a major part. The benefits of the codification approach is the reuse of knowledge, as knowledge can be codified and thus stored in databases for all employees to use, and that knowledge is shared through people to documents approach. The second viewpoint, the personalization approach, derives from linking people through networks to facilitate the sharing of tacit knowledge.

Hansen et al (1999) place the codification approach along with companies that produce standardized products, for example standards and guidance used within the audit firm. The personalized approach is seen to be more suited to companies that customize solutions to fit unique problems, for example when an audit firm perform audits, no client companies will appear the same and knowledge will be shared mostly by people to people contact.

The study of Hansen et al (1999) provided evidence that Anderson Consulting, before its collapse in 2002, and Ernst & Young focused on the codification approach by developing various ways to codify, store and reuse knowledge. Employees could retrieve interview guides, benchmark data, different documents on various analyses and work schedules creating a database with a large scale reuse of codified knowledge without having to contact the original person who developed the document. However, the codified approach was not the only approach used in the two audit firms who were the subjects of the study. There was people to people contact as well, but Hansen et al (1999) found the high degree of emphasis on codified knowledge striking. As knowledge is reused in an effective way the audit firm saves work which will reduce costs and allowing an audit firm to take on more clients. This was evident as Ernst & Young could increase revenues from 1.5 billion dollars to 2.7 million dollars from the year 1995 to the year 1997 (Hansen et al, 1999).



## 3.5 Organizational learning

Organizational learning as a concept can be viewed parallel to knowledge management (Sallis & Jones, 2002), or as Jaschapara (2004) puts it:

*“The literature of organizational learning is much more mature than the relatively recent literatures of the ‘learning organization’ and ‘knowledge management’ and provides an essential cornerstone for the emerging knowledge management literature”* (Jaschapara, 2004 page 59).

Advocates of knowledge management refer to the ability of learning in a company as an important factor for success. As knowledge management can be seen as how a company can codify and store, share and transfer, use and reuse the knowledge and information supplied, organizational learning refers to how a company can create knowledge and how a company can learn (Sallis & Jones, 2002).

This may be of interest as we are focusing the study on three global audit firms, operating around the world with multiple cultures, and there might be different learning preferences, as the firms exceed over 135 000 (Ernst & Young homepage: Our people – delivering on our promises) respective 165 000 employees (Deloitte homepage: Facts & Figures) and 155 000 employees (PricewaterhouseCoopers homepage: Company fact).

When facing a familiar problem the solution usually lies with the creation of organizational routines deriving from existing knowledge. The organizational routines within a company are stored as procedural memory in the company as routines are seen to exist of tacit knowledge (Jaschapara, 2004).

There are two different perspectives of organizational learning (Finnbäck et al, 2008). The first perspective believes that companies have various types of knowledge. Tsoukas (1996) defines this approach as the taxonomic approach. Researchers in the taxonomic field believe that it is possible to identify various forms of knowledge, and then analyse the implications of each identified form of knowledge. Through identifying and defining various forms of knowledge a more effective way of sharing, transferring and usage of knowledge can be found. The

most prominent distinction of knowledge is that of explicit and tacit knowledge which was presented by Polanyi in the late 1950<sup>th</sup> (Ibert, 2007). Tsoukas (1996) use the classification of knowledge to develop strategies or routines where the knowledge is either created, codified or transferred.

The other perspective of organizational learning is critical to the taxonomic approach as they preach that it is not possible to systematically divide and classify knowledge (Finnbäck et al, 2008). One criticism is that the taxonomic approach does not take into account that organizational knowledge is built as an integration of explicit and implicit knowledge (Tsoukas, 1996). Brown and Duguid (1998) support Tsoukas view, however, they do not split knowledge into explicit and implicit knowledge. They rather refer to Ryle's, from 1949, definitions of knowing how, know-how, and knowing that, the ability to use know-how in practice (Finnbäck et al, 2008).

# 4 The structure and the use of IFRS

In this chapter we will lay the basis we will need to be able to analyze the empirical data of how the audit firms implement IFRS. We will illustrate the structure and use of IFRS. This chapter will also include a presentation of Mary Tokar’s article regarding KPMG and Anders Bäckström’s article describing the application of IFRS in Sweden.

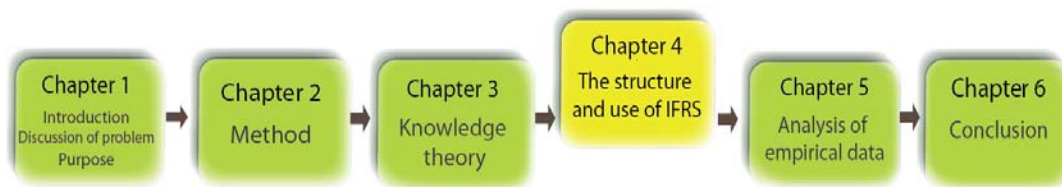


Figure 4: Disposition guide

## 4.1 International Accounting Standards Board

To have effective and functioning capital markets, the role of financial information is essential for the global economy and an important element in the financial information architecture is the set of financial reporting standards (Ball, 2004). International Accounting Standards Board (IASB), situated in London, is an independent standard setter

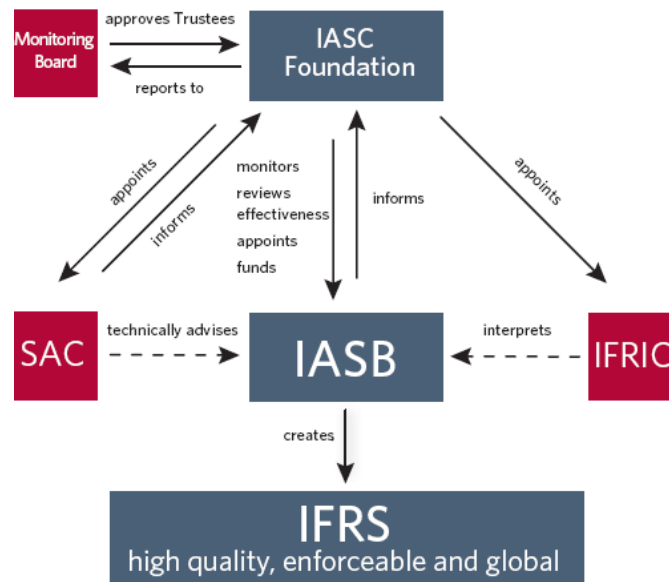


Figure 5, The organization of IASB (IASB paper: Who are we and what do we do)

who provides common financial reporting standards to the world’s capital

markets. In 2001, IASB replaced the International Accounting Standards Committee (IASC) (Deloitte homepage: What is the IASB). IASB is appointed and overseen by IASC Foundation (see Figure 5) which was created in 2000 and whose responsibilities are governance and fund-raising to IASB (Ball, 2004). The IASC Foundation is in turn accountable to capital market authorities through a Monitoring Board. The IASB is also supported by SAC (Standards Advisory Council) and IFRIC (interpretations committee) who provides guidance when divergence occurs i.e. they promote consistent application.

According to IASB, since 2001, over 100 countries require or permit the use of IFRS. There are also countries that are seeking convergence with, or pursuing adoption of IFRS (IASB paper: Who are we and what do we do). In 2002 the European Union approved a regulation to adopt IFRS for listed companies in the EU for their consolidated financial statements in 2005, called the EU Regulation 1606/2002 (Nobes & Parker, 2008). Another highlight was in 2006 when IASB and FASB agreed upon a roadmap for convergence between IFRS and US GAAP and then, in 2008, US published a roadmap for IFRS adoption (IASB paper: Who are we and what do we do).

When applying the IFRS system the countries in EU could choose between different adoption methods. The different adoption methods are indirect or direct adoption. Direct adoption is adoption of IFRS instead of national GAAP and indirect adoption is changing the national standards so they are based on IFRS or in some cases, copied directly from IFRS. When EU adopted IFRS, they planned for a direct adoption of IFRS however, it has lately become in part an indirect adoption of some standards and thus created a form of EU GAAP. There are other countries that have permitted or required the use of IFRS without reviewing the standards and these are Australia, Russia and some Latin American- and Caribbean countries (Tokar, 2005).

## 4.2 The structure of IFRS system

As Whittington (2005) puts it, the development of IFRS derives from the demands from the capital markets. He argues that the development of IFRS is free from political incentives from governments or other bodies however, there are those who disagree. Nobes and Parker (2008) claim that the IFRS was partly set up to counter the American dominance by strengthening the capital markets of EU.

The collapse of Enron led to a wide debate on what accounting approach should be used. The US GAAP was considered to be overly dependent on rules, details and guidance instead of letting principles or professional judgement rule (Tweedie, 2005).

The IFRS is perceived by many to be principles based (Schipper, 2003). What distinguishes principles based from rules based seems to be that principles based standards are not well defined and can vary in different interpretations (Bennett, Bradbury & Prangnell, 2006). According to Schipper (2003) the principles based international accounting system allows or even requires the use of professional judgement.

One of the main differences between principles based and rules based is the check-box mentality which is dominant in the rules based accounting system (Schipper, 2003). Even if the check-box mentality is seen as a negative attribute of the rules based system the advantage is that compliance with the rules can easily be monitored and enforced (Dewing & Russell, 2004). The main advantage of the principles based accounting system is that it is based on judgement when evaluating the effects of a series of transactions (Overbeek, van Apeldoorn & Nölke, 2007), with few bright-line definitions (Benston, Bromwich & Wagenhofer, 2006). However, the downside is that decisions may not be clear cut and there will be room for professional disagreement (Overbeek et al, 2007).

## **4.3 The use of IFRS**

IFRS have a lot of users and the practice of IFRS can differ among countries, industries and companies. We will in this section try to explain a couple of differences when using IFRS globally. According to Nobes and Parker (2008) there are eight different categories of scope for different IFRS; different versions of IFRS, different translations, gaps in IFRS, overt options, covert options, measurement estimation, transitional issues and imperfect environment. We will only illustrate six of these factors which can be connected to our main research question.

### **4.3.1 Different translations**

There are international differences in the application of IFRS. SEC has found about 30 different versions of IFRS that have been established by local and regional jurisdictions (Erchinger & Melcher, 2007). Tsakumis, Campbell, & Doupnik (2009) point out two factors that could hinder interpretation and application of IFRS, one of them being translation. Nobes (1998) made a simile between a company's accounting practices and a human being. According to him, the number of practices can be seen as infinite when referring to a company's accounting practice (just like the manners of human individuals). Although there exists several practices (all species are different), there are certain common features. According to Tsakumis et al (2009) differences in translations could result in lack of comparability between countries even though they apply the same international accounting system.

The IASB issues and approves its work written in the English language. Therefore, the translations of IFRS, guidance, interpretations and other official publications are a vital part of achieving a common international accounting system (IASB homepage: Translation). The purpose of the creation of an international accounting system was to eliminate barriers in communication by

having different national languages of accounting (Whittington, 2005). However, there is a risk that when translating from English to a national language, for example within the EU, the translation can change the meaning from the original version (Nobes & Parker, 2008).

The IASB has published their official translation process and policies which are based on two parts. The first part is professional translation where key terms are extracted and translated by professional translators. The second part of the translation is letting a committee of accounting experts review the translation. The members of the committee have the specific language as their native language and have proven knowledge expertise in a particular area of IFRS (IASB Homepage: Official translation process and policies).

#### **4.3.1.1 Cultural effects on translations and interpretations**

According to Gladwin and Hofstede (1981) culture matters and national culture effects both organizations and organizational behaviour theories. People have mental programs which affect peoples' perceptions, beliefs and behaviour both within and outside the organization. They argue that these characteristics are predictable.

Differences in translations could be connected with cultural differences or problems (Doupnik & Richter, 2004). This may be a problem as the EU has given the translated version of IFRS legal status in the member states (Nobes & Parker, 2008).

Various differences in international accounting are present in today's global environment. Nobes and Parker (2008) list a number of reasons; culture, legal systems, providers of finance, taxation, other external influences and the profession. However, Nobes (1998) previous work states the concept of culture being the key factor. He suggests the six characteristics described above all derive from culture rather than being independent variables. The main reason for differences, according to Nobes (1998), would instead depend on if the country is

culturally self-sufficient, depending on the outsider equity market, or whether the country is culturally dominated, when culture determines the accounting system.

In 2006, Douppnik and Riccio addressed a more general question as topic for their study, whether culture could cause different interpretations in different countries who apply the same accounting standards. They found that there was substantial support for culture effecting verbal probability expressions referring both to income recognition and when disclosure should be made. As a result, Douppnik and Riccio (2006) state that values in national culture may affect how accountants interpret IFRS probability expressions which may lead to variations in decisions based on when to recognize income and when to disclose information. The accounting culture in an audit firm can vary if an employee works with one of the Big Four audit firms or if the individual is employed by another firm (Douppnik & Riccio, 2006).

#### **4.3.2 Overt options**

As noted before, the purpose of accepting and implementing IFRS is to remove the transnational accounting differences. However, in some accounting standards there are several options when choosing an appropriate accounting method which will result in that international accounting difference will always remain due to overt options. An example of overt options is IAS 2, 25 §, whether to chose FIFO (First In First Out) or weighted average cost when determining the cost of the inventories (Nobes & Parker, 2008).

#### **4.3.3 Covert options**

Covert options or a vague criterion could be the use of the term *probable* which could be interpreted differently. For example in Germany they interpret the word *probable* more conservative than in the US (Douppnik & Richter, 2003 and Douppnik & Richter, 2004). Another example is IAS 28, 2 §, where it states that



identification with an associate should be based on *significant influence*, the question is, how much is significant? Nobes and Parker (2008) describe another view of covert options which is the existence of IFRIC and they believe that IFRIC is an evidence of the possibility for different interpretations of the standards. Since IASB publishes principle based standards instead of rules based standards, it means that IASB do not want to have strictly detailed standards (Nobes & Parker, 2008).

#### **4.3.4 Measurement estimations**

In IFRS there are some measurement estimations that have to be made, for example when accounting for depreciation, where the preparer have to estimate the assets expected useful lifetime. Another example of measurement estimations is fair value for certain financial assets and liabilities in IAS 39, 48 § (Nobes & Parker, 2008). Another example is given by Rosen (2008) who considers the problems associated with IFRS when testing for impairment of long term assets. He claims that executives may write up the value of the specific asset to an amount they decide on when adopting IFRS. The executives then keep the value at the artificial level cashing out stock options (Rosen, 2008). However, a study conducted in 2007 showed differences in measurement not only within IFRS but also between IFRS and US GAAP. The study found that IFRS increased income, investment returns as well as other financial measures and that more than 80 percent of the company's net income and returns on equity was higher under IFRS than US GAAP (Malwitz & O'Rourke, 2009).

#### **4.3.5 Imperfect enforcement**

Making companies de facto conduct high quality financial statements and to follow IFRS, cannot solely be achieved through a regulatory requirement (the 2002 EU regulation, 1606/2002). The regulations have lead to the establishment

of enforcement bodies (Brown & Tarca, 2005). The degree of enforcement is a problem when using IFRS since enforcement is a national matter when complying with IFRS (Nobes & Parker, 2008). Challenges the enforcement bodies have had to face are the different structures and responsibilities for oversight which are different within the EU member states (Brown & Tarca, 2005). This can lead to different financial statements since some countries do not have an enforcer and those jurisdictions who have an enforcer work in different ways. Efforts have been made to increase cross-jurisdictions securities regulations in EU however, this cannot be compared to the creation of one single enforcement body (Schipper, 2005).

## **4.4 Handling IFRS issues in Sweden**

Bäckström (2009) claims that the use of IFRS is here to stay however, achieving comparability will be a big challenge. He implies that the importance lies in trying to affect in what direction IFRS is heading and to use IFRS in a reasonable and a sensible way. Bäckström believes that the introduction of IFRS has changed the conditions for auditors, and the implementation of IFRS has led to the liberation for auditors. The auditors criticize and try to affect IFRS which is shown as audit firms around the world are eagerly commenting on standards and publications. When it comes to setting norms and the everyday work for auditors the move to IFRS has led to a shift in power, from a national level to an international level. Also, there has been a shift of power from the individual auditor to the audit firm and into the international networks where the audit firm is a member. It has also led to an increasing demand for specialization and experts within IFRS. In every conducted audit, technical expertise in IFRS is a necessary component and it is common that employees functions as IFRS expert within the audit firm and whose responsibilities are to double check the financial statement before approving the audit (Bäckström, 2009).

#### **4.4.1 Networks and International helpdesks**

To make sure that information and knowledge of interpretations and implementations from the global firm reaches the individual national firms the audit firms have set up a global network. Bäckström (2009) describes the routines generally accepted within the audit firms when dealing with problems of interpretations or implementations. He mentions that the Swedish audit firms have national, technical, specific departments to deal with such issues within the firm. These departments consist of 20-30 employees with technical accounting expertise as well as an international IFRS Contact Partner. Also, it is not unusual that the audit firms have an IFRS Reviewing Partner. The Reviewing Partner does not participate in the audit but rather acts like an adviser when the audit team requires support. When stumbling across an issue which the audit team cannot solve, a possible solution is first discussed with the Swedish department of specialists of IFRS or with the IFRS Contact Partner. These bodies need to decide if the issue should and could be solved within the team, office or if the issue needs to be sent off to the audit firm's international department of experts. The centres specialized in IFRS are usually based in London (Bäckström, 2009).

When an issue is to be dealt with through the audit firm's global specialized IFRS department, the procedure turns complicated and the issue is documented according to a specific and strict routine. The documentation includes different opinions and arguments from clients, the audit team and the national department's technical accounting expertise (Bäckström, 2009).

The Panel of Experts are involved if a problem or issue sent to the London department is seen as too complex and cannot be solved internally. Within the London department the Panel of Experts get involved in either of the three following cases; when a question is principally important to either the client or the specific country of the client, when the question risks the auditor to leave a qualified report or when the question seems too important or sensitive that an analysis by the panel is necessary. The Panel is also responsible for approving the comment letters on outcasts of standards and other publications (Bäckström, 2009).

An audits firm's policies of IFRS are established by the Panel of Experts. Their main purpose is to make official statements in complex IFRS issues that are not covered in any publications or any previous rulings. The statements from the Panel of Experts are binding for the audit firm. Communication between the Big Four audit firms' international London department is important to reach a general agreement upon interpretations. If not, the goal of increasing comparability could vanish quickly (Bäckström, 2009).

#### **4.4.2 Global Public Policy Symposium**

To achieve a unanimous voice within the audit profession, a global network was created among a number of audit firms. The Global Public Policy Symposium (GPPS) is arranged by the six largest international audit firms; PricewaterhouseCoopers, Ernst & Young, Deloitte, KPMG, BDO and Grant Thornton. The goal is to create an international network to discuss critical issues in both financial reporting and auditing as an attempt to get audit firms and other organizations to try to strive in the same direction. The fourth GPPS meeting brought together over 250 members from around the world representing regulatory-, investor-, corporate- and professional communities (Global Public Policy Symposium homepage: Welcome). Sweden was represented by both the Revisorsnämnden and representatives from the audit firms (Engerstedt, 2008).

#### **4.5 An example: KPMG**

Tokar (2005) describes in her paper how KPMG has built an infrastructure through their global network concerning IFRS. The Big Four audit firms have supported the application, development and adoption of IFRS. Tokar (2005) describes that one of the biggest challenges with IFRS is to coordinate day-to-day activities in the 140 independent and separate national member firms. In other

words, the challenges are how to have one single, integrated voice while the legal entities still remain separate and independent.

Tokar (2005) poles up some key implementation issues in her paper; training professionals in IFRS, avoiding divergence through different interpretation, developing publications and electronic resources, adapting existing quality control, and coordinating the participation in the standard-setting process. KPMG has addressed these issues by the creation of a global IFRS department to achieve a more consistent interpretation and application in all of their national member firms. The Big Four audit firms have all invested in training. To confront the issue of training professionals KPMG has added IFRS training to their local training requirements by translating and developing material.

According to Tokar (2005) it is very important that the audit firms translate materials into the local languages and at the same time develop the training and planning in IFRS. The divergence through different interpretation is important because to achieve a common view of IFRS, the member firms and the global network firms have to interpret the standards similarly. Tokar argues that experiences show that IFRS can be read and interpreted differently due to which national GAAP and culture the preparer has. As described in previous part, IFRIC is not an urgent body and do not solve problems quickly and it takes about one year for IFRIC to develop an interpretation. Because of this, KPMG has created a supplement to IFRIC with an own interpretation body of IFRS and have attempted to distribute the IFRS capabilities to their local member firms. This interpretation body publishes material for both internal and external use (Tokar, 2005).

As previously mentioned the indirect and the direct adoption of IFRS create a couple of challenges for auditors as well as their audit firms and these challenges are to: train the professional staff, develop IFRS based resources to support the staff and apply quality controls to IFRS based work. Countries that use the direct adoption of IFRS often face problems since there is no corresponding regulatory framework or infrastructure around IFRS and auditors and companies have to change their internally practices when preparing the financial statements (Tokar, 2005).

## 4.6 IFRIC

As mentioned before, the International Financial Reporting Interpretations Committee (IFRIC) is IASB's interpretation body and tackles accounting problems that are of broad importance and problems that:

*"...are likely to receive divergence or inconsistent treatment in the absence of authoritative guidance..."* (Ball, 2004).

The interpretations produced by IFRIC have the same legal status as IFRS (Bradbury, 2007).

IASB describe IFRIC as a non urgent group and their focus is more on the *due process* because IASB do not desire a large number of interpretations. IFRIC's base is a principle approach and they are:

*"Not seeking to create an extensive rule-oriented environment"* (Bradbury, 2007).

This has resulted in that the interpretation problems not taken into IFRIC's agenda are more than the interpretations IFRIC produce.

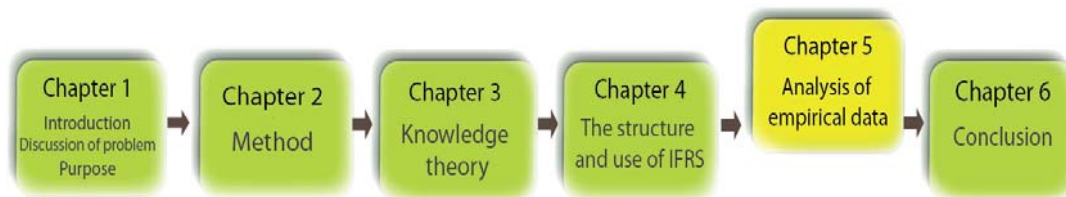
A problem with the IFRIC and other interpretations groups, especially national interpretations, is that the other interpretations bodies will handle the problems that arise and these interpretations may conflict or be inconsistent with IFRIC's interpretations (Bradbury, 2007). Tokar (2005) also highlights this problem if a national interpretive body interprets a standard that is inconsistent with IFRIC or other national interpretive bodies.

# 5 Empirics and analysis

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In this chapter we present the empirical data we will need to analyze how an audit firm implements IFRS as well as how the firm then shares this knowledge throughout the organization. Under each empirical theme we will analyze the results based on the theories presented in chapters four and five. In the beginning of this chapter we will present information about the three audit firms.

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*Figure 6: Disposition guide*

The answers from the interviews with the three audit firms' respondents will be described according to the questions in the interview guide (see Appendix A or B). We will only address relevant parts of the respondents' answers which we found important and interesting to give a better base for the analysis. When compiling and interpreting our empirical data we have tried to be as unbiased as possible to not affect the results and our ambition is to retail the citations and abstracts in its right context and not have any scores in it.

We have divided this chapter into different themes and in each theme we will present the empirical data from the interviews. In every theme there will be an analysis based upon the empirical data and theories that we illustrated in earlier chapters.

To be able to fully comprehend the analysis of the empirical data we will present information of the three case companies; PricewaterhouseCoopers, Deloitte and Ernst & Young, to better understand how they function and how they are structured on both a global and national basis.

## **5.1 Information about the case companies**

We have chosen to study three audit firms; Deloitte, PricewaterhouseCoopers and Ernst & Young, which are included in the Big Four audit firms. The Big Four audit firms are located all over the world and the firms provide similar services such as audit, consulting, tax and financial advice. Since the Big Four audit firms are nowadays the main interpreters of IFRS and because the firms interpret IFRS separately this can lead to different financial statements within the EU, therefore the Big Four audit firms are interesting to study.

Another argument for choosing these audit firms are when a regular user wants information about IFRS, the audit firms; Deloitte, PricewaterhouseCoopers and Ernst & Young, differ when providing such information. Deloitte and PricewaterhouseCoopers have set up homepages where they provide summaries and reports about IFRS and any user can take part of this information while Ernst & Young's knowledge base about IFRS is password protected on their homepage. Because Ernst & Young do not share their information about IFRS while Deloitte and PricewaterhouseCoopers do, we have chosen to compare the three audit firm's implementation and knowledge transfer.

### **5.1.1 Organizational structure of the three audit firms**

To find out whether there are differences between the three of the Big Four audit firms' implementations and knowledge transfer of IFRS, we need to understand how the Big Four audit firm's organizational structure looks like. We will present the three firms separately and describe the nature of the global networks and their national member firms.

#### **5.1.1.1 Deloitte**

In 2008, Deloitte had 165 000 employees located in 140 countries (Deloitte homepage: Facts & Figures). In Sweden, Deloitte has 1 100 employees and 37



offices (Deloitte homepage: Statistics). Deloitte has a network of legal, separate and independent member firms that are members in Deloitte Touche Tohmatsu (DTT). DTT is a Swiss legal person and do not provide any services, instead they coordinate activities with all of their member firms around the globe. The independent member firms work in a specific geographical area where they follow the national laws and regulations (Deloitte homepage: About us). On Deloitte's homepage they describe the relationship between the member firms and DTT as:

*“Deloitte Touche Tohmatsu and the member firms are separate legal entities responsible only for their own actions”* (Deloitte homepage: About us).

#### **5.1.1.2 PricewaterhouseCoopers**

PricewaterhouseCoopers have 155 000 employees and are located in 153 countries around the world. In Sweden they have 3 400 employees and are situated in 125 locations (PricewaterhouseCoopers homepage: Company fact). PricewaterhouseCoopers are structured as a network of member firms to PricewaterhouseCoopers International Limited (PwCIL). PwCIL is based in UK and does not provide any services, instead they identify opportunities, develop strategies, promote PricewaterhouseCoopers, develop and work for consistent application of quality standards by member firms which also include compliance. To be a member of PwCIL, the national firms have to have locally qualified professionals who have majority or full ownership in the firm which means that all member firms are locally owned and managed (PricewaterhouseCoopers homepage: How we are structured). On PricewaterhouseCoopers homepage they describe the relationship between the member firms as:

*“PricewaterhouseCoopers refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity”* (PricewaterhouseCoopers homepage: How we are structured).

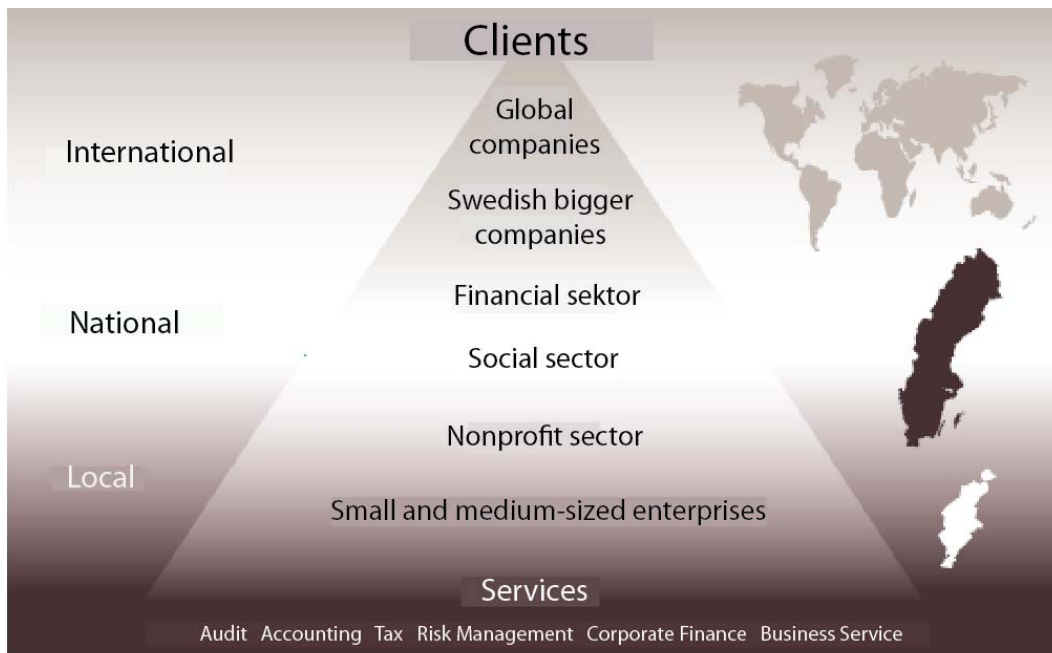


Figure 7, PricewaterhouseCoopers' services and clients  
(PricewaterhouseCoopers annual review 2006-2007)

Figure 7 illustrates how PricewaterhouseCoopers are structured in Sweden and the figure describes how auditing differs between various kinds of clients.

### 5.1.1.3 Ernst & Young

Ernst & Young are included in the Ernst & Young Global Limited which is a global network of member firms. Ernst & Young provide services in 140 countries and have 130 000 employees globally (Ernst & Young homepage: About us). Ernst & Young are situated in 70 locations and they have about 1 800 employees in Sweden (Ernst & Young annual review 2006/2007). The member firms are directly or indirectly members of Ernst & Young Global Limited (EYG) or Ernst & Young International, Ltd (EYI). EYG is a UK private company and work as a principal governance entity to the global Ernst & Young organization and do not provide any services. Ernst & Young describe the relationship between the member firms and EYG on their homepage as:

*“Each of EYG and its member firms is a separate legal entity and has no liability for another such entity's acts or omissions”* (Ernst & Young homepage: Bottom of the page).

## **5.2 Knowledge and knowledge transfer**

In this section we will present the respondent's answers focusing on knowledge and knowledge transfer of IFRS in the three audit firms. We will first describe each of the respondents' answers and thereafter present our analysis.

### **5.2.1 PricewaterhouseCoopers**

According to the respondent at PricewaterhouseCoopers they use different methods when transferring knowledge within their firm. They have databases available for the employees and they also have courses every year to update the employees' knowledge in different subject areas. The differences when PricewaterhouseCoopers transfer knowledge concerning Swedish rules and IFRS are not many. The difference is that they use, with the exception of databases and internal courses, different publications where they spread their line of thoughts and interpretations which have arisen from various issues within IFRS on a more international basis than if an issue concerns the national GAAP.

The respondent from PricewaterhouseCoopers also mentioned that PricewaterhouseCoopers have produced a book called "Manual of Accounting". According to the respondent each of the Big Four audit firms has produced this kind of book. In the book, "Manual of Accounting", PricewaterhouseCoopers have written how they think in certain matters and the book is available for everyone. Deloitte, Ernst & Young and KPMG have also issued manuals of accounting where they have stated what they think in certain matters. The respondent also believes that it is quite easy to get information concerning IFRS because of the databases and the publications which every employee has access to.

In summary, when they transfer knowledge regarding IFRS, PricewaterhouseCoopers use databases, publications and internal courses. Because PricewaterhouseCoopers is a big firm, they use mostly internally generated

material however, they also assimilate themselves with publications from IASB or other materials according to the respondent.

### **5.2.2 Deloitte**

Deloitte uses annual organized courses within the firm, for example when implementing new laws, and they also use newsletters and updates to share information. For auditors newly acquainted with IFRS they have web-based courses where the auditor goes through every IFRS recommendation. According to the respondent from Deloitte, she perceives IFRS as more as on the “job training” compared to other Swedish accounting regulations. When graduating from the university, Deloitte have more audit methodology training than IFRS courses and it is when the need arises an auditor attend courses about IFRS. However, partners, managers and even senior management at Deloitte attend regular updates on new recommendations.

The respondent from Deloitte also adds that knowledge can be transferred when the employee ask its coworkers about different problems which the coworkers might have encountered before. Deloitte have landscape offices which, according to Deloitte’s respondent, promote the exchange and transferring of knowledge. They work in teams in which they can ask other members when questions arise. Transferring information about IFRS within Deloitte does not differ from transferring other information, except they use FAR SRS, their Intranet and Deloitte’s international IAS Plus homepage. The respondent does not find it hard to acquire information about IFRS due to the web-based courses and IAS Plus homepage.

To sum up, Deloitte use databases (intranet), publications, courses and newsletters when they transfer knowledge. Deloitte use a mixture of internally generated material and official publications. They use official recommendations when to understand certain situations while the internal materials such as newsletters are used to keep the employees updated. But when the employees encounter a problem they go foremost to the official publications.

### **5.2.3 Ernst & Young**

According to the respondent at Ernst & Young the most common form of transferring knowledge are databases, newsletters, knowledge lunches and internal courses. At Ernst & Young every employee attend initial courses about IFRS and when the employee wants or requires deeper information about IFRS he or she can take additional courses within different subject areas. These courses can be taken internally in Sweden or abroad within the global organization, or such as IREV courses.

The information regarding IFRS are collected in a database that every employee at Ernst & Young has access to and this database includes both international material and national material from Sweden. There is a department at Ernst & Young who publishes newsletters about current accounting issues within the IFRS area. They also have, as mentioned before, knowledge lunches and internal courses when transferring information about IFRS. The respondent from Ernst & Young states that the firm uses both internal and official publications when using IFRS.

The respondent finds it easy to get information about IFRS due to the database. However, the respondent adds that for the employees who are not working with IFRS, it can be hard to find or to assimilate the international material and instead they should contact the department of technical expertise.

### **5.2.4 Analysis and discussion**

In accordance with Alvesson (2004, referred in Finnbäck et al, 2008), each audit firms' respondent mentioned that knowledge is transferred within the organization through various channels. Alvesson claims that a characteristic of a knowledge intensive company is how the organization use advanced knowledge and the main comparative advantage lies in finding an effective method to use the intellectual capital (Finnbäck et al, 2008). The most commonly used channel within Deloitte, Ernst & Young and PricewaterhouseCoopers is through databases without

neglecting the importance of other sources, for example courses and newsletters. It is important that Deloitte, Ernst & Young and PricewaterhouseCoopers support the most effective ways of gathering and sorting information to transform and share knowledge so the embedded knowledge will not be wasted, a risk highlighted by Vera-Muñuz et al (2006).

Further evidence that Deloitte, Ernst & Young and PricewaterhouseCoopers are knowledge intensive companies is that their employees are highly educated, in accordance with Finnbäck et al (2008), and that they attend ongoing courses in IFRS to expand their knowledge capital.

Davenport et al (1998) also explained how the multiple channels contribute to the effectiveness of knowledge transferring. As Deloitte, Ernst & Young and PricewaterhouseCoopers highlight in the interviews, there is not one way of sharing data, information or knowledge but many. The knowledge flows out in the organization, through databases, through newsletters, through courses, through interacting in the team or within the office or using other means of communication and the knowledge is used by those who require it. All of the respondents said that the respective audit firm uses multiple channels rather than one, which strengthens Davenport et al's (1998) argument that one channel does not reduce the need for another but that they rather reinforce each other.

#### **5.2.4.1 Uncodified sources for knowledge transfer**

As Vera-Muñuz et al (2006) mentioned, when performing an audit each individual must perform to succeed. To be able to succeed, all knowledge and the expertise required to perform has to be either embedded within the individual or just an arm's length away. Vera-Muñuz et al (2006) believe that knowledge and expertise needs to be shared among the audit firms' employees and within the teams. Deloitte, Ernst & Young and PricewaterhouseCoopers all conduct audits based on team work and all respondents mentioned that the communication within the team is important to maximize and utilize the knowledge each individual, team and office possess. Braff's (2000) second perspective, knowledge management as a strategic tool, can be illustrated through for example Deloitte's open landscapes

(having no fixed office spaces) and how Deloitte, Ernst & Young and PricewaterhouseCoopers always work in teams.

According to Ribiere (2009) the organizational culture and the employees' motivation to share or acquire information is important. If not, the quality of the incentives or tools to communicate or transfer knowledge within the company is irrelevant and the knowledge will be lost. Even though the codified proportion of the information and knowledge stored within the organization is high, the respondent of Deloitte highlighted the informal exchange and transfer of knowledge within the team and the office.

The personalization approach, sharing of tacit knowledge, is more suitable when dealing for example with customized client solutions. Asking questions and other ways of informal personalized communication can be connected to Malone (2002) who claimed that there is more knowledge embedded in the employees of respective audit firm than there is documented. When sharing tacit knowledge the information or knowledge is transferred from one individual to another. It is important to have Sveiby's (1995) reasoning in mind where he states that the information one individual extends to another may not be the same that the other accepts or creates. This can create variations between individuals' implementation and application of IFRS.

#### **5.2.4.2 Factors affecting knowledge**

Another of Davenport et al's (1998) factors which is evident from the interviews with Deloitte, Ernst & Young and PricewaterhouseCoopers, and Tokar's (2005) article of KPMG, is that it seems clear that the respective senior management support the knowledge management system. This argument is based on the development of teamwork, courses and different educations the employees at all levels are required to attend and the wide spread of databases throughout the organizations.

Davenport et al (1998) identified senior management support as a factor affecting the effectiveness of knowledge. The support from the senior management is

important as a part of letting the employees know how important sharing knowledge and learning is to the companies' success by setting the tone for a knowledge oriented organizational culture. The respondents mentioned how everyone in respective audit firm attend courses on a regular basis to develop additional knowledge to their previous experience as well as receiving new information when changes in standards and other material has been made. If the higher level of employees (senior partners, management etc.) continuously tries to acquire knowledge and information, this sets an example for the rest of the firm creating a knowledge friendly culture as well as a clear notion for senior management support.

A few of Davenport et al's (1998) factors affecting the effectiveness of knowledge can be linked to the audit firms' transfer of knowledge. The factor of standard and flexible knowledge structure can be connected with the audit firms. This is a prerequisite for sharing and transferring knowledge because if the audit firms' database would for example lack a clear structure and be unorganized, lacking categories or keywords, the employees' retrieval of the knowledge or information needed would be hindered. Deloitte, Ernst & Young and PricewaterhouseCoopers have databases where an employee can search for whatever information the individual may seek regarding IFRS. The respondents of Deloitte, Ernst & Young and PricewaterhouseCoopers found it to be easy to locate the information one needed however, as respondent from Ernst & Young mentioned, it might be harder for an unpractised employee to collect relevant information.

Davenport et al (1998) also stated the importance of a knowledge friendly culture and the support of the senior management to achieve an organizational culture which affects knowledge. The respondent of Deloitte mentioned that they work in landscapes and teams which promote the exchange of knowledge between them and they share a lot of knowledge. If one does not know the answer or solution to a specific issue you ask around to see if someone has encountered such a problem before. The fact that the employees work in teams means that there is always someone to ask or use as a sounding board. This factor is also supported by Ribiere (2009) who believes that Deloitte, Ernst & Young and PricewaterhouseCoopers can use an organizational culture which is positive to



sharing and acquiring knowledge as an advantage and this will have a positive impact on knowledge sharing.

#### **5.2.4.3 Codified knowledge**

Knowledge management emphasizes the part of creating, handling, storing, using, reusing, sharing, transferring and acquiring knowledge that may impact the respective audit firm's ability to transfer knowledge. It was evident in Deloitte, Ernst & Young and PricewaterhouseCoopers that codified knowledge is the base for and the general way of transferring knowledge without diminishing the part personalized knowledge plays.

According to the information we received through the interviews, the handling of information and knowledge is shared through various forms using the Internet. Braf (2000) divided knowledge management into two perspectives. The information management tool dealt with collecting and storing the individual's knowledge which then can be shared to other employees within the organization. This can be connected with Deloitte, Ernst & Young and PricewaterhouseCoopers use of databases when sharing information.

When talking to respective respondent it becomes clear that the audit firms believe knowledge can be stored, retrieved and used through for example databases, courses and newsletters. This approach supports the taxonomic approach of knowledge where it is possible to identify and define various forms of knowledge and therefore develop more effective ways of sharing, transferring and usage of knowledge (Tsoukas, 1996 and Ibert, 2007). Explicit knowledge is codified and stored, mainly through databases. Deloitte, Ernst & Young and PricewaterhouseCoopers all store information and knowledge in various forms of documents and facilitate the retrieval of these documents with the use of for example databases.

The use of databases, which is evident in Deloitte, Ernst & Young and PricewaterhouseCoopers, supports the codification approach within knowledge management (Ribiere, 2009). The codification approach is a major part of audit

firms. Hansen et al (1999) presented a study which emphasized the part played by codified knowledge within audit firms. This became clear when we analysed the collected empirical data as all respondents underlined the use of databases and documents. Furner et al (2009) stated that when a company relies heavily on information and knowledge being transferred and shared within the company the outcome of learning is correlated with how the KMS is designed. Deloitte, Ernst & Young and PricewaterhouseCoopers did not mention the specific arrangement of the databases more than that they found them easy to use.

As Jaschpara (2004) notes, the solution lies within organizational routines which can be used to store procedural memory. When facing a familiar problem the employee can seek existing resources, namely the databases. The respondents noted that all employees have access to the databases if and when they require information, which enhances Vera-Muñoz et al (2006) notion of all needed knowledge and expertise having to be just an arm's length away.

When the audit firms transfer knowledge through for example databases and newsletters it is done via the Internet. The respondent of Deloitte also mentioned web-based courses in IFRS. It focuses on the people to documents approach and would imply that Deloitte, Ernst & Young and PricewaterhouseCoopers codifies and stores knowledge in databases. There might be a risk that the documentations of information and knowledge turn into *noise*, a risk highlighted by Rooney (2003). However, the Deloitte, Ernst & Young, PricewaterhouseCoopers respondents did not find that the information regarding IFRS was difficult to find due to the databases, the web-based courses and the Deloitte website IAS Plus.

It is also evident that because of the principles based accounting system; Deloitte, Ernst & Young and PricewaterhouseCoopers, all have created manuals of accounting to specify how each audit firm wants to interpret and apply the IFRS standards. The respondents mentioned the use of both internally generated materials, for example these manuals of accounting, as well as official publications. As Evangelist and Hau (2009) explained, explicit knowledge is highly codified, articulated which can be transferred in systematic language. The documented form of information and knowledge stored in these manuals are

available for everyone as an attempt to show how IFRS is supposed to be interpreted, implemented and applied.

However, the respondent from Deloitte viewed IFRS as more of on the “job training”. This refers to the knowledge stored in the audit firm to be more than just codified knowledge. The knowledge was created when working with IFRS and in that way generating experience in the area. The ability to perform a practical task without the ability to explain the action in words is one definition of tacit knowledge (Finnbäck et al, 2008). When an employee performs audits he or she generates knowledge through experience and the task becomes more as a job training. It is imbedded within the individual, becoming a valuable resource to the audit firm. Sveiby (1995) presented a study showing that the most effective way of remembering is achieved when an individual performs or does something in practice.

## **5.3 Complications with IFRS**

We will in the following section present our empirical data regarding IFRS. Together with the empirical data and the previously presented theories we will analyze and understand the context in which the audit firms use IFRS.

### **5.3.1 PricewaterhouseCoopers**

According to the respondent from PricewaterhouseCoopers, they have a central coordination and interpretation function in London which is located at a central level. The function is situated in London for the reason that the IASB also is located in London and thereby PricewaterhouseCoopers can have a close relationship with IFRS. Since PricewaterhouseCoopers have a global network of member firms they have to cooperate on a central level. When problems occur when interpreting IFRS they have to have:

*“A coordinated operation in which we address the problems on a central level if we do not think we can solve it on a local level”* (Respondent from PricewaterhouseCoopers).

When using IFRS an employee from PricewaterhouseCoopers is supported by annual courses for auditors in shape of updates, advanced courses and there is also a possibility to attend courses which are not organized internally. Another support for the auditors when using IFRS at PricewaterhouseCoopers is the proximity to IFRS experts. Since only listed companies have to use IFRS in Sweden, these companies are often located in the bigger cities. If the company is listed at Stockholm stock exchange they are often located in Stockholm and in other big cities in Sweden such as Malmö and Gothenburg. Therefore PricewaterhouseCoopers only have representatives of IFRS experts in these three cities but mostly in Stockholm. If an employee identifies a problem, he or she should turn to the department of accounting specialists (IFRS experts) where they:

*“...discuss the issue and jointly arrive at a solution that we deliver to our clients”* (Respondent from PricewaterhouseCoopers).

### **5.3.2 Deloitte**

Deloitte also have a support system with IFRS experts. They have one IFRS expert situated in Malmö and the rest of the IFRS experts are situated in Stockholm. In Gothenburg there are a lot of people who have experience with IFRS but not any full-time experts. The respondent from Deloitte said that they have a department who work with financial reporting as a support for the auditors and this department has a large knowledgebase about IFRS. The department is located in Stockholm and supports everyone who works with IFRS questions within Deloitte in Sweden. However, according to the respondent from Deloitte, when an auditor has to interpret the standards, the auditor often has a direct dialogue with other employees working with accounting questions. Ultimately, it is the authorized auditor who signs the audit report and who takes the decisions.

As a result, the employee always has some kind of support within Deloitte. At the office in Malmö they have one IFRS expert and the respondent from Deloitte said:

*“Being close to him here, I think, is very positive, it is always easier to walk by his office and throw him a question rather than to call someone in another office.”*

(Respondent from Deloitte).

When an employee at Deloitte faces uncertainties or interpretation problems the employee turns to the department of experts, his or hers team or read the recommendations from IFRS. The respondent from Deloitte said that sometimes the Swedish translations are odd which makes it hard to understand the standard and then you have to go back to the English version of IFRS to distinguish what the intention of the standard is. The respondent finds it disturbing that sometimes it is not enough to read the Swedish version and it is an unnecessary interpretation to read the English material.

Deloitte has an IFRS unit and helpdesk in UK and it is this unit who are responsible for the IAS Plus homepage. When you are working with international companies in Sweden some questions escalate to them. The respondent from Deloitte said that IFRS is a complex system of rules and the rules should cover all companies, from the largest to the smallest listed companies, and emphasizes that there are big differences in the questions and complexity depending on the company.

### **5.3.3 Ernst & Young**

Ernst & Young has a Global IFRS Policy Committee in London who publishes for example “International GAAP” which is guidance when using IFRS in practice and the Global IFRS Policy Committee also publishes “IFRS Questions and Answers”. When an employee in Sweden encounters problems or interpretation difficulties they should primarily turn to the Technical Department of Ernst & Young in Stockholm. For certain specific questions, Technical Department can also turn to the unit in London for more guidance according to the respondent.

IFRS experts within Technical Department work primarily from Stockholm but there are also experts in Gothenburg and Malmö.

### **5.3.4 Different interpretations of IFRS**

When interpreting standards they can sometimes vary when interpreting different words or sentences. On the question whether the interpretations between the Big Four audit firms can differ, the respondent from PricewaterhouseCoopers answered:

*“Often it is the standard itself that is vague and unclear”* (Respondent from PricewaterhouseCoopers).

The respondent continues with that the problems often are resolved by contacting IFRIC or IASB to try to clear out the vagueness. On the other hand, the respondent from PricewaterhouseCoopers also states that there must be room for interpretations due to IFRS being a principle based set of regulations and therefore different audit firms will come up with different conclusions.

The respondent from Deloitte explained that every firm tries to create a firm practice and the Big Four audit firms try to cooperate for example through FAR SRS and they try to have a common view on certain problems. The respondent states that from different conditions certain standards can be interpreted in different ways and the respondent adds that we are all individuals which lead to that there will always be different interpretations in different audit firms.

Ernst & Young’s respondent answered that there are differences in the interpretation of different IFRS for the reason that:

*“IFRS is a principle based system and it is quite natural with different interpretations”* (Respondent from Ernst & Young).

### **5.3.5 Analysis and discussion**

Nobes and Parker (2008) list differences in IFRS and these can be connected to the creation of general accounting policies and manuals for the interpretations and other accounting issues within the respective audit firm. The Big Four audit firms are all organized under one global organization but all member firms operate as separate legal entities. Even though the liability within the global network is decreased; policies, standards, guidance and interpretations, are to be followed throughout the global organization to be able to meet the requirements of today's international companies and to create consistencies when implementing and applying IFRS throughout the organization. If the interpretation of a standard is the same in one country as another it will facilitate the audit.

#### **5.3.5.1 Diverse interpretations**

The interpretations made within each audit firm are to be followed throughout the whole firm. Organizational learning deals with how an organization creates knowledge (Sallis & Jones, 2002) which can be related to how audit firms interpret different standards and guidance. When an interpretation is created information is shared and received. All of the respondents believe that there might be differences in interpretations between the audit firms. One of the respondents said:

*“...I have no good example, but we are all different as individuals, so there are probably differences in the interpretations”* (Respondent from Deloitte).

If, according to Douppnik and Ritcher (2004), one individual's interpretations are dependent on his or hers culture there should be differences in interpretations. Another viewpoint is Nobes (1998) who claims the number of accounting practices can be related to the number of companies. If each company conducts its accounting in its own way, the respondent from Deloitte's perspective regarding humans being different as individuals' diverse interpretations will be made.

Coordinated interpretations are required because of the audit firms' global networks. Tokar (2005) described that KPMG has set up the global IFRS group as an attempt to address divergence through different interpretations; they develop publications for the organization to follow (e.g. accounting manuals), electronic resources (databases) and coordinate when KPMG participate in standard setting processes (e.g. approving comment letter sent to IASB). Bäckström (2009) use the same motives for the creation of these global IFRS groups. The respondent from PricewaterhouseCoopers mentioned that their firm's national IFRS group set the approach that PricewaterhouseCoopers considers to be acceptable from an IFRS perspective. As Ernst & Young has set up the EY Global IFRS Policy Committee in London to publish internally generated materials, it is clear that the audit firms want to prevent different interpretations and implementations of IFRS.

#### **5.3.5.2 Problem with translations**

However, Nobes and Parker (1998) mentioned that problems might arise due to different translations. The respondent of Deloitte mentioned how there might arise situations where an auditor needs to go to the original version of IFRS (the English version) because the translations were not understandable. The fact that these translated versions of IFRS, for example in Swedish, are hard to comprehend, but still have legal status, would demonstrate why different interpretations arise even though the IASB has produced a strategy to avoid these complications (IASB homepage: Translations). Tokar (2005) also mentioned the importance translating the publications of IFRS into local languages. Even though the IASB have an official policy on translation of any publications (IASB homepage: Official translation process and policies), for example with accounting experts in the native language involved in the process, IASB will not be able to stop different interpretations from arising if the translation is not written in a clear way as the respondent of Deloitte commented on.



### **5.3.5.3 Internally generated material**

One reason for the audit firms' creation of internally generated materials is, as previously mentioned, because IFRS is based on principles. When an individual interprets and applies a standard it is not certain that the result will be the same as if another employee from the same firm would have applied the standard. The respondent from PricewaterhouseCoopers noted that it is not unusual with different conclusions in a principles based regulatory framework. The respondent continues:

*"...otherwise we have a rules based interpretations that says what to do or what not to do, and that is what we do not wish for. So, there must be room for interpretation"* (Respondent from PricewaterhouseCoopers).

In general, IFRS is seen as a principle based accounting system (Schipper, 2003). The use of professional judgment is significant when applying IFRS and as Dewing and Russell (Overbeek et al, 2007) highlight decisions are not always clear cut which can result in professional disagreement. As the knowledge of IFRS is embedded in the employees' individual experiences and professional skills implementations and interpretations may vary. Deloitte, Ernst & Young and PricewaterhouseCoopers all expressed that because IFRS is built on principles it will differ, both internally and between audit firms.

The respondent from Deloitte underlines that respective audit firm tries to have some form of a generally agreed upon agency praxis. In accordance with Bäckström (2009), the Big Four audit firms' policies of IFRS are created in London and are applicable for all member firms within respective global network. Many audit firms have created accounting manuals where the audit firms' opinions and way of perceiving a specific issue is stated. Since Bennett et al (2006) argue that the standards of IFRS are not well defined and therefore vary in different interpretations, this might add to the reasons for generating internal material for the respective audit firm to follow. This was evident when the respondent from PricewaterhouseCoopers mentioned the creation of and the use of these accounting manuals. The accounting manuals are also presented on the websites of Deloitte and PricewaterhouseCoopers. These accounting manuals are

produced to help prevent the emergence of different interpretations as the audit firms' accounting manual tries to achieve a common or generally agreed upon opinion when encountering accounting issues. However, the manuals can have the opposite effect as they may create differences in implementation and interpretation of IFRS between audit firms.

If each firm creates policies of accounting without making sure they are not contributing to the increasing gaps and different versions of IFRS this will result in problems. Instead of reaching a homogeneous and a common accounting system four more versions of IFRS (one for every Big Four audit firm) will be created in addition to the 30 different versions found by Erchinger and Melcher (2007). This is why the Global Public Policy Symposium is important because it creates a forum for discussion as well as organizing the six largest audit firms to go in the same direction (Global Public Policy Symposium Homepage).

#### **5.3.5.4 IFRS experts**

Before reaching out to the respective helpdesk, the problems are dealt within the IFRS expert groups at the local or national level. This is of course if the problem is not solved within the audit team or office as the respondent of Deloitte mentioned. Bäckström (2009) described the working process when dealing with an IFRS issue in the same way as the respondents from both Deloitte and PricewaterhouseCoopers. The respondents from Deloitte, Ernst & Young and PricewaterhouseCoopers mentioned that the proximity of the national or local IFRS group of experts supporting auditors work with IFRS was positive. The respondent from Deloitte focused on the close connection with an IFRS expert in the office which made it easier to solve tricky accounting issues and who works as an IFRS Reviewing Partner (focusing on IFRS, not conducting audits), a function within the Big Four audit firms mentioned by Bäckström (2009). According to Bäckström, it is the group of IFRS experts or the IFRS Contact partner who needs to decide whether the issue can be solved locally or needs to be sent to the international IFRS expertise department which was also mentioned by the respondent from PricewaterhouseCoopers.

Knowledge, as in unarticulated or non-verbalized knowledge, embedded within for example a team member or an IFRS expert is tacit knowledge (Evangelista & Hau, 2009). The respondent from Deloitte highlights that it is easier to ask a question within the team or to the IFRS expert situated in the Malmö office instead of calling or in other ways contacting various experts for the answer to the specific question. According to scholars (Finnbäck et al referring to: Realin, 1998; Pleasants, 1996; Kalling & Sthyre, 2003), this would imply that the transferring of implicit knowledge in some part is connected to the individual's eloquence.

#### **5.3.5.5 IFRS departments in London**

We did not get specifics of the process of contacting the international departments of experts. The respondents described briefly that an individual of the team would contact an expert within the office, or otherwise reach out to the national IFRS group of experts whom has the possibility to ask for support with the international IFRS department in London. This procedure seemed to be quite similar in the audit firms, Deloitte, Ernst & Young and PricewaterhouseCoopers, and in accordance with Bäckström (2009) who tried to map out this process.

In the interviews with Deloitte, Ernst & Young and PricewaterhouseCoopers the respondents mentioned the international helpdesks. The audit firms have their helpdesk located in London. Because the helpdesks coordinate the global networks interpretations of IFRS, its work should have a huge impact on respective audit firm. There are external factors that the audit firm cannot affect. Nobes (1998) list six variables which he claims all derive from culture. This would imply that the interpretations made in for example the accounting manuals would be affected by the underlying culture of the country or jurisdiction. The respondent from PricewaterhouseCoopers mentioned that they may not agree with all the official guidelines and interpretations made but they must abide by the official directives. However, the audit firms all participate in the development of IFRS and try to affect IFRIC's work through issuing comment letters. Bäckström (2009) mentioned that comment letters are approved by the respective audit firms London department's Panel of Experts. According to the respondent from

PricewaterhouseCoopers the reason that the office of the global network is situated in London is to be close to the IASB.

The helpdesk is contacted if the national IFRS group cannot find a solution to the problem according to the respondent from PricewaterhouseCoopers. Bäckström (2009) claims that all Big Four audit firms work in similar ways when dealing with issues of IFRS. Bäckström noted three cases where the global IFRS helpdesk is contacted; when it is principally important, when there is a risk of leaving a qualified report or when the issue is important or of a sensitive matter. These statements are consistent with the respondent of PricewaterhouseCoopers asserting that one of the reasons for contacting the global IFRS group is when an issue has precedent value. It is the audit firms' international interpretation bodies that produce the internally accepted material on IFRS to be used within the respective firm, according to both Tokar (2005), Bäckström (2009) and the respondent from PricewaterhouseCoopers.

An important aspect of the international IFRS departments in London is that they conduct the respective audit firms' accounting policies and accounting manuals. The respondent from Ernst & Young mentioned that the Policy Committee in London issues recommendations as practical guidance when applying IFRS. The respondent from PricewaterhouseCoopers also highlights the publications from the centralized IFRS department. As a result, the policies made in London are supposed to suite every jurisdiction. These are to be followed and the policies are binding for all member firms, no matter what jurisdiction the member firm operates in. This can be troublesome since IFRS is a principle based accounting system that requires interpretation of the standards, which when translated or applied may result in different translations or interpretations than what was originally intended. What is interesting to note is the Douppnik and Riccio (2006) study which found that the member firms of the Big Four audit firms' audits may differ from other audit firms outside the Big Four, even though they operate in the same country.

### **5.3.5.6 Centralization and decentralization**

The degree of centralization affects how information and knowledge is shared within the audit firms. As noted previously, Alvesson (2004, referred to in Finnbäck et al, 2008) characterizes knowledge intensive firms to have a more decentralized organizational structure which makes the information and knowledge flow easier throughout the organization. However, as noted in Bäckström's (2009) article and confirmed by the respondents from Deloitte, Ernst & Young and PricewaterhouseCoopers, each of the Big Four audit firms have chosen to have one centralized IFRS support office based in UK. One argument is the desire to be close to IASB in London. Another argument, expressed by Tokar (2005) is when the audit firms set up national, technical, specific departments for IFRS the need for support and coordination for each national department of expertise was recognized which lead to the creation of a global IFRS resource group.

Bäckström (2009) also mentioned that in Sweden the statements from the panel of experts (IFRS experts) in the Big Four audit firms are binding which suggest a decentralized organization, and at the same time, a centralized organization. As the respondent from PricewaterhouseCoopers pointed out, if they are not able to solve the problem on a local level, they should turn to the central or global level when a problem arises. Once again an individual can perceive the reality differently and it depends on what kind of view an individual has when deciding whether the audit firms' transfer of knowledge is centralized or not. A local Swedish firm maybe see the knowledge process as centralized when the interpretation is made in Stockholm while the person in Stockholm finds it centralized when the interpretation is made in London (see figure 4).

The indirect evidence of a centralized organization, within the knowledge and information area, is the international IFRS department of Deloitte, Ernst & Young and PricewaterhouseCoopers. Also, the general accounting principles and manuals are issued by the respective audit firms' international IFRS departments to be used throughout the global network of member firms. Another example is the respondent from Ernst & Young who preferred to run our answers through an

expert as a way to answer our questions in accordance with the audit firm's guideline.

Tokar (2005) states that KPMG has decentralized their IFRS capabilities to their local firms rather than having one single location as they wanted to integrate IFRS with the existing structure of the member firms because KPMG wanted to continue "business as usual" when using the IFRS. KPMG then developed a professional practice function in each country as they have implemented IFRS as the core competencies to the member firm. This is evident as the national technical experts in IFRS within Deloitte, Ernst & Young and PricewaterhouseCoopers are represented in a few offices. However, it is not possible to have an expert in every local member firm as the respondents pointed out.

## 5.4 Quality controls

Ernst & Young have quality controls at different levels. Within an audit team, a team member's work is always reviewed by a superior person. They have also other reviews made by independent persons with a certain periodicity. Their IFRS control of the financial statements is:

*"Before the audit report is released the required financial statements are subject to a so-called technical review, i.e. it is reviewed by a person highly qualified within IFRS"* (Respondent from Ernst & Young).

The quality controls of IFRS at PricewaterhouseCoopers are:

*"That senior people have the right to sign this type of document which will become a formal interpretation from PwC"* (Respondent from PricewaterhouseCoopers).

At PricewaterhouseCoopers all audits have to go through senior partners and as the respondent said:

*“It is aligned at the international level if it would be so prejudicial in a case that they consider the need for information on international plan around this”*  
(Respondent from PricewaterhouseCoopers).

The respondent from Deloitte had a similar answer and said that all IFRS annual reports should go through their group of experts.

#### **5.4.1 Analysis and discussion**

Bäckström (2009) mentioned that every conducted audit is overseen by an expert in IFRS whose responsibility is to double check the audit before it is approved and signed. This in line with the statements of the respondents from Deloitte, Ernst & Young and PricewaterhouseCoopers who all highlight that a highly qualified person will review the audit before it is approved.

Once again, the fact that IFRS is a principles based accounting system, may affect the interpretations of the standards. In contrast to US GAAP, which is more rules based, interpretations and the use of professional judgments is the basis of IFRS (Schipper, 2003 and Tweedie, 2005). The respondent from PricewaterhouseCoopers highlights the fact that the IASB does not wish to make IFRS into a strict and rules based accounting system, but the consequence of this will of course be that interpretations, implementation and application of the standards and guidance will differ. This is also reported by Bradbury (2007) claiming that IFRIC are not seeking to create a rule based accounting environment. The reasons above are motives why it is important that the Big Four audit firms' quality controls are successful because the quality controls will facilitate a consistent application within each firm and decrease the possibility for different interpretations.

Consistency is an important part of keeping the quality of the conducted audits intact, both within the firm and externally. Within the respective audit firm the existence of official accounting policies and manuals, as described previously,

helps achieve the goal of consistency. Externally, the GPPS assists the largest audit firms to keep within a general line of business.

The ability to control compliance of IFRS can be difficult as the respondent from Deloitte said:

*“...to make a valuation, if you have three different valuation institutes then you can reach three different proposals on how the accounting can look like”*  
(Respondent from Deloitte).

This can be related to the advantage with the rules based US GAAP, it is easier to monitor and control if a company complies with the standards when following the check box mentality than what is possible with the principle based IFRS (Schipper, 2003).

The lack of a common enforcer may affect the quality controls of IFRS. It is up to each jurisdiction to set up a well function enforcer body (Nobes & Parker, 2008). Brown and Tarca (2005) also argue that the different structures and responsibilities of enforcement bodies within the EU have led to challenges and inconsistencies. If a country in the EU lacks a functioning enforcer, the risk of different interpretation increases. On the other side, since the Big Four audit firms are located in every country in the EU and in almost every city, the lack of an enforcer is not as necessary because if the audit firms have functioning quality controls in each member firm will lead to the risk of different interpretations in EU decreases.

As we attempt to study the three audit firms' Swedish member firms the enforcement is equal for all. The internal quality controls were similar within all three audit firms. The respondents from both Deloitte and PricewaterhouseCoopers mentioned that it is only senior people who have the right to sign the audit report. Deloitte and Ernst & Young also stated that the audit is required to pass through their internal group of IFRS experts.

The quality controls that the respondents mentioned are in line with Bäckström's (2009) description of the audit process within a Swedish Big Four audit firm. The respondent from PricewaterhouseCoopers explains how an issue or problem



which the national technical IFRS department of experts cannot handle or is believed to have a precedent value is sent to the London department of IFRS experts. This is a strategy to make sure that new issues are dealt with correctly from the beginning so that the interpretations and application of standards are the same. The verdicts of the London IFRS department of experts are binding according to Bäckström (2009).

## **5.5 Problems with IFRS standards**

The respondent from PricewaterhouseCoopers believes that the most problematic standard in IFRS is the IAS 39 *Financial instruments*. This standard has been criticized which has led to more updates and clarifications how to use the standard especially in the current financial crisis.

Deloitte's respondent believes the standards which leaves room for interpretations such as impairment and provisions are most the problematic. Many recommendations are "square" and a user has to draw assumptions to be able to follow the standards. The assumptions are not mentioned in the standards which lead to the user having to estimate which percentage or time horizon to apply. As a conclusion, there are a lot of standards where a user has to appreciate certain factors and that are the hardest and problematic part in IFRS according to the respondent from Deloitte.

Ernst & Young's respondent also believe that IAS 39 *Financial instrument* is the most problematic and adds that financial instruments in it selves are complex which makes the accounting difficult and complex.

### **5.5.1 Analysis and discussion**

As mentioned previously, Nobes and Parker (2008) stated various obstacles to homogeneous interpretations. Obstacles are found in standards that are based on

measurement estimations, when dealing with covert or overt options and when using a translated version of IFRS. The respondent from Deloitte mentioned that these were the kind of factors that makes it difficult to interpret a standard ‘correctly’ and in a consistent manner.

The respondents from Deloitte, Ernst & Young and PricewaterhouseCoopers noted the standards which require estimations as problematic. Nobes and Parker (2008) as well as Rosen (2008) highlight the problems with measurement estimations. The respondent of Deloitte claimed that even if the standard itself is clear (for example no covert or overt options) problems arise if the standard is based on calculations and estimations which will differ in how one individual interprets for example useful lifetime.

The respondent from Deloitte also commented on the difficulties when estimating which percentage and when taking the time horizon into account when conducting an audit in accordance with IFRS. Rosen (2008) highlights some problems that may arise when applying the IFRS rules. He gives an example of how executives might write up the value when testing for impairment of long term assets. This is supported by Dewing and Russell (Overbeek et al, 2007) who claim that professional disagreement will arise when professionals have to decide how to interpret or apply a complex or vague standard. This might explain why the respondent from Deloitte feels that there is a part of insecurity when estimating as there is no ‘real’ answer to what and how an interpretation of a standard shall be made.

The fact that IFRS is based on principles may give rise to different interpretations, not only between individuals but also between different audit firms.

*“...in a principles based regulatory framework it is not surprising that one can come to different conclusions”* (Respondent from PricewaterhouseCoopers).

The respondents from Ernst & Young replied that due to IFRS being principles based accounting system it is quite natural with different interpretations. A similar response came from Deloitte’s representative.

IAS 39 of IFRS as endorsed by EU has been an object for carve outs (Dewing & Russell, 2008). IFRIC has published an interpretation but are working on amendments (Deloitte homepage: IFRIC 9) and still all three respondents from the different audit firms mentioned this standard as a complex and difficult standard. The respondent from Ernst & Young argues that because financial instruments themselves are complex it sometimes makes the accounting of them complex and difficult.

## 5.6 IFRIC

*“IFRIC is an agency who work to clarify when there are significant problems of interpretation”* (Respondent from PricewaterhouseCoopers).

The respondent continues with that sometimes they agree with IFRIC and sometimes they do not. When they do not agree they often submit a response. When a statement from IFRIC is released it is just to apply the standards as any other standards said the respondent from PricewaterhouseCoopers. They have to use IFRIC’s statement because they cannot turn against a statement which is supported by the EU.

Deloitte’s respondent uses IFRIC’s statement:

*“To the extent they are applicable”* (Respondent from Deloitte).

The respondent from Deloitte said that IFRIC’s statement have not been very important to her personally but maybe in the future.

Ernst & Young’s respondent states that IFRIC has a difficult mission since they get a lot of questions but can only treat a few of the problems. The respondent continues that they have to use IFRIC’s interpretations since it is a part of IFRS.

### 5.6.1 Analysis and discussion

As Bradbury (2007) notes, the IFRIC statements have legal status and therefore the interpretations made by this body are of the same importance as the individual standards and guidance produced by the IASB. This can be connected with one of the respondent's comments on how they have to follow an official statement from IFRIC regardless if they agree with the statement or not. However, the respondent from Deloitte states that the IFRIC's statements have not been particularly important to her. As Bradbury and the respondent from Ernst & Young argue, the IFRIC does not give out many statements because the interpretive body does not desire a great deal of interpretations. This might be seen as a contradiction when IFRS is a principles based regulatory framework and interpretations of standards and other materials are a must. On the other hand, because interpretations made by IFRIC have legal status, interpretations will become rules.

As Schipper (2003) claimed, principles based accounting standards will always be dependent on the level of professional judgment. The respondent from Deloitte mentioned that they need to interpret the standards, especially standards which require the use of measurements and estimations, leaving the de facto interpretations of a standard to the auditor and thus on the individual's level of professional judgment and not to IFRIC.

The respondent from PricewaterhouseCoopers mentioned that the much debated IAS 39 *Financial Instruments* is perceived as the most difficult standard to comprehend. IFRIC 9 *Reassessment of Embedded Derivatives* was released in 2006 but amendments have been discussed since (Deloitte homepage: IFRIC 9). Still it is considered as one of the most difficult standards. Once again, if the users do not feel that the IFRIC statement clarifies how to apply the standard the de facto interpretations on implementing and applying IAS 39 will fall on the audit firms.

# 6 Conclusion

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In this chapter we are going to summarize and present the conclusions we have reached on the basis of the material presented earlier in this study. We are also going to relate our empirical findings with the purpose and our research question. We close this chapter by giving suggestions for further research.

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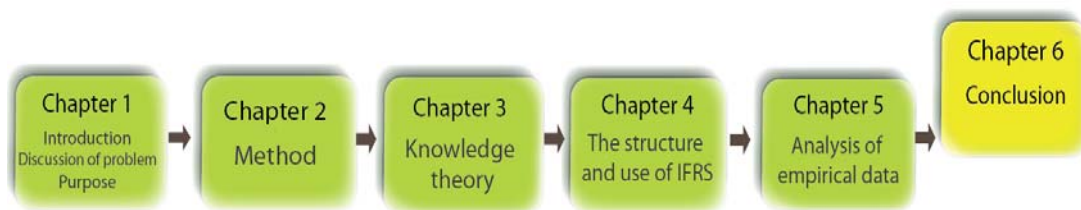


Figure 8: Disposition guide

## 6.1 Concluding remarks

The purpose of this thesis was to identify similarities and differences in implementation and application of IFRS in the Big Four audit firms. In order to do this we are going to see how interpretations of IFRS are shared and transferred within the audit firms. By using Tokar's (2005) article describing KPMG's implementation issues we aim to answer our purpose and research question in this section.

It becomes evident that the audit firms are knowledge intensive companies as the audit firms use knowledge throughout their organization as a basis for their operations. Through gathering and sorting knowledge and information they make knowledge accessible for everyone within their organization regardless if they use the codified- or the person to person approach. When transferring and implementing knowledge they use multiple channels such as databases, newsletters, courses, teams and manuals. When analyzing our empirical data it was clear that there are more similarities between the audit firms when

transferring and implementing knowledge than there are differences. We found that they used the same channels when transferring knowledge however, we cannot determine whether they use the channels to the same extent.

In our findings we can draw a conclusion that a possible scenario is that the audit firms create their own way of dealing with insecurities regarding IFRS. Audit firms' accounting manuals, their courses and educations as well as their every day work conducting audits, require taking decisions on how to interpret and apply the standards. Some standards demand the employee to make estimations of certain variables, which can indirectly create an individual interpretation and implementation approach of the standard in use.

Tokar (2005) poled up some key implementation problems that are similar to the problems we have brought up in this thesis. The problems, as previously mentioned are: training professionals in IFRS, to avoid divergence through different interpretation, to develop publications and electronic resources, and to adapt quality controls.

When referring to the respective audit firms' education system, it is clear that training professionals in IFRS has become a key to success. We believe the reason that the education system is important is because the knowledge process facilitates when the employees are well informed and educated when interpreting and applying standards in such a complex accounting system as IFRS is viewed to be. All audit firms emphasized on that all of the employees, including senior management, should attend courses, both to keep the employees updated and to keep up with newly issued standards and guidance. We believe this creates presumptions for a knowledge friendly culture which impregnates the entire organization.

Avoiding divergence through different interpretations is another factor presented by Tokar (2005). We found that one of the reasons behind the different interpretations and implementation of IFRS is the individuals' patterns of life which is an evident factor to why the employees interpret standards differently, especially since IFRS is based on principles and requires the use of professional judgment. Other factors that affect different interpretations made by the audit

firms are the translations of IFRS which the audit firms have solved through internal generally agreed upon policies. These policies are made and transferred by the audit firms' IFRS experts who are binding for the member firms to avoid inconsistencies. In our opinion, it is not surprising that generally agreed upon interpretations, both regarding IASB and their internal material, will be hard to achieve as the layers of individuals' previously perceived reality will affect the outcome.

It became clear that when an issue arises the aim is to solve the problem close to the nearest instance of the hierarchical support chain to smoothen the process. An issue is at firsthand solved within the team or office which tends to a decentralized organization. If the problem cannot be solved locally they reach out to the national IFRS experts which are supported, in specific cases, by the global department of experts which is a characteristic of a centralized organization.

The three audit firms have developed publications and electronic resources because there are a lot of information regarding IFRS that need to be transferred. To be able to utilize and share the information in the most effective way the audit firms have set up databases. All firms have also issued a manual of accounting to achieve consistency when implementing IFRS and to avoid inconsistencies in interpretations. In our findings there are no differences between the audit firms regarding the use of databases and publications. We believe that codified information is an essential part of an audit firm. Also, apart from the high amount of the codified information and knowledge, all audit firms work in teams and we have found that the informal transfer of knowledge is part of the process when conducting an audit. The informal knowledge is often transferred through landscapes, persons to persons and teams.

Adapting quality controls involves IFRS experts, reviewing partners and seniors signing the audit report. The audit firms have IFRS experts as a support for consistent implementation when conducting an audit. A part of the quality control is having a highly qualified person who reviews that the financial statements and the audit report are in accordance with IFRS. If the national firm encounters a problem which has not been dealt with before, the issue is sent to the London

department of IFRS experts. This is especially important when an issue is seen to have precedent value so the global experts can interpret the standards and then transfers the interpretation to national member firms to avoid inconsistencies when interpreting and implementing IFRS. We believe the quality controls have an impact on the creation of the formal interpretation that is going to be followed throughout the organization and to create high quality and consistent audits in the member firms.

To highlight our theoretical contribution, we believe that we have made a clearer picture of how the knowledge and transferring of IFRS are used in the three audit firms. There do not exist many differences, if any, in the audit firms ways of transferring knowledge and information. However, as mentioned before the interpretations can differ between the audit firms because the IFRS is a principle based accounting system and we are all individuals with different patterns of life. The reasons that the audit firms are similar when transferring knowledge and information might be that they already have found effective channels. Unfortunately, we have not found to which extent these channels are used but the channel of databases is the most important factor when storing all audit firms knowledge of IFRS according to us. The general technical development has affected the environment for auditors and has helped them to become more cost and knowledge efficient. Also, the fact that they are included in the Big Four audit firms with similar services, organizational structure, policies etc it is not surprising that they are transferring and sharing information and knowledge in similar ways. The similarities can as well be dependent on the audit firms' cooperation on a high level and since the cooperation between the audit firms in GPPS and FAR SRRS as we all as in the global networks, probably have eliminated most of the largest differences when the member firms implement and apply IFRS. Another reason is their loads of internal material and courses which have helped to create consistency among the member firms when an individual auditor conducts audits.

These concluding remarks of similarities between the audit firms only relate to the transferring of knowledge of IFRS. Nevertheless, we believe that audit firms



might differ on a deeper level and in different subject areas within the audit firms' organizations.

## **6.2 Continued research**

We have not been able to determine if the audit firms use different channels when transferring information or knowledge in the same extent. This could be done by a closer observation or survey focusing on how much they utilize different channels. Suggestions on different channels that could be studied are: teams, documents, internal courses etc.

A suggestion on continued research is to consider, compare and analyze the internally generated material in respective audit firm to see if there are any more differences with emphasis on databases. All firms highlight the importance of databases and therefore it would be interesting to see whether the information and structure of the databases are similar.

Another proposal of continued research would be to see how the information de facto flows in the organization. This could be done via close observations of the audit firms to map out how information and knowledge are transferred within the national firms or the whole global network.

An additional research can be conducted through studying the organizational context of the audit firms to compare how this affects the transfer of knowledge. The focus of the research can be to see how decentralized or centralized the audit firms are in different areas. The views could be from a local national member firm, the headquarters of the national member firm or from the global network.

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## Figures

Figure 1: Disposition guide (Self-composed)

Figure 2: Disposition guide (Self-composed)

Figure 3: Disposition guide (Self-composed)

Figure 4: Disposition guide (Self-composed)

Figure 5: International Accounting Standards Board (IASB) paper: *Who are we and what do we do*, April 2009 [http://www.iasb.org/NR/rdonlyres/95C54002-7796-4E23-A327-28D23D2F55EA/0/WhoWeAre\\_Revise5Feb09.pdf](http://www.iasb.org/NR/rdonlyres/95C54002-7796-4E23-A327-28D23D2F55EA/0/WhoWeAre_Revise5Feb09.pdf)

Figure 6: Disposition guide (Self-composed)

Figure 7: PricewaterhouseCoopers annual review 2006-2007 Sweden  
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Figure 8: Disposition guide (Self-composed)

# Appendix A

## Intervjuguide

### Personlig bakgrund samt anställning

- Hur länge har du varit anställd?
- Vad är din titel?
- Vad är dina huvudsakliga arbetsuppgifter?
- Hur sprids kunskap på er byrå? Vilken form är den mest vanligaste? (ex databaser?)

### IFRS

- Har ni en central tolkningsenhet av IFRS- standarder? Isf var och hur?
- Vem tolkar standarder i IFRS som ska följas inom företaget?
- Hur sprids exempelvis nya IFRS- standarder och tolkningar inom företaget?
- Vilken utbildning får en anställd på er byrå i IFRS? Vilket stöd får en revisor i IFRS regler på er revisionsfirma?
- Finns det IFRS- experter på varje kontor och/eller på varje avdelning?
- Är det lätt för en anställd att skaffa sig information om IFRS?
- Hur hanterar en anställd hos er oklarheter och tolkningssvårigheter i hanteringen av IFRS? Vart vänder den anställde sig?
- Vad finns det för material tillgängligt om IFRS för revisorer på er byrå?
- Vad har ni för kvalitetskontroller när det gäller IFRS hos er?
- Vilken standard i IFRS anser byrån är mest problematisk? Hur visar det sig?
- Finns det skillnader i tolkningen av IFRS mellan revisionsbyråer? Om ja, inom vilka områden? I vilken utsträckning? Om ja, vad anser du är anledningen?
- Hur ser er byrå på IFRICs arbetsuppgifter? Och vad anser byrån om deras tolkningar? Använder ni dem?

- När det gäller IFRS, använder byrån till största del internt upparbetat material eller officiella publikationer inom området?
- Är er byrå, eller någon anställd på byrån, involverad i den *samhälliga* debatten kring tolkningsfrågan? Om ja, någon på detta kontoret?

# Appendix B

## Interview Guide

### **Personal background and employment**

- How long have you been employed?
- What is your title?
- What are your main tasks?
- How is knowledge shared in your firm? What form is the most common? (E.g. data bases)

### **IFRS**

- Do you have a central interpretation unit of IFRS standards? If so, where and how?
- Who interprets standards of IFRS that are to be followed within the company?
- How are e.g. new IFRS standards and interpretations shared within the company?
- What education regarding IFRS is an employee given at your firm? What kind of support does an auditor get from IFRS rules within your firm?
- Are there IFRS experts in each office and / or in each department?
- Is it easy for an employee to obtain information about IFRS?
- How does an employee handle doubts and difficulties of interpretation when dealing with IFRS? Where does the employee turn to?
- What are the materials available on IFRS for auditors in your firm?
- What is your quality control in terms of IFRS within the firm?
- What standard of IFRS does the firm believe to be most problematic? How does it show?
- Are there differences in the interpretation of IFRS between different audit firms? If yes, in what areas? To what extent? If yes, what do you think is the underlying reason?

- What is your firms' opinion on the work of IFRIC? And what do the firm think of their interpretations? Do you use them?
- In the case of IFRS, does your firm use for the most part internally generated material or official publications within the field?
- Is your office, or any employee of the firm, involved in the societal debate regarding the question of interpretations? If so, someone in this office?