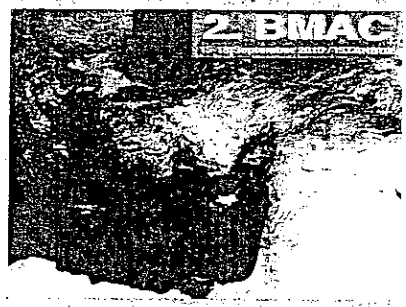
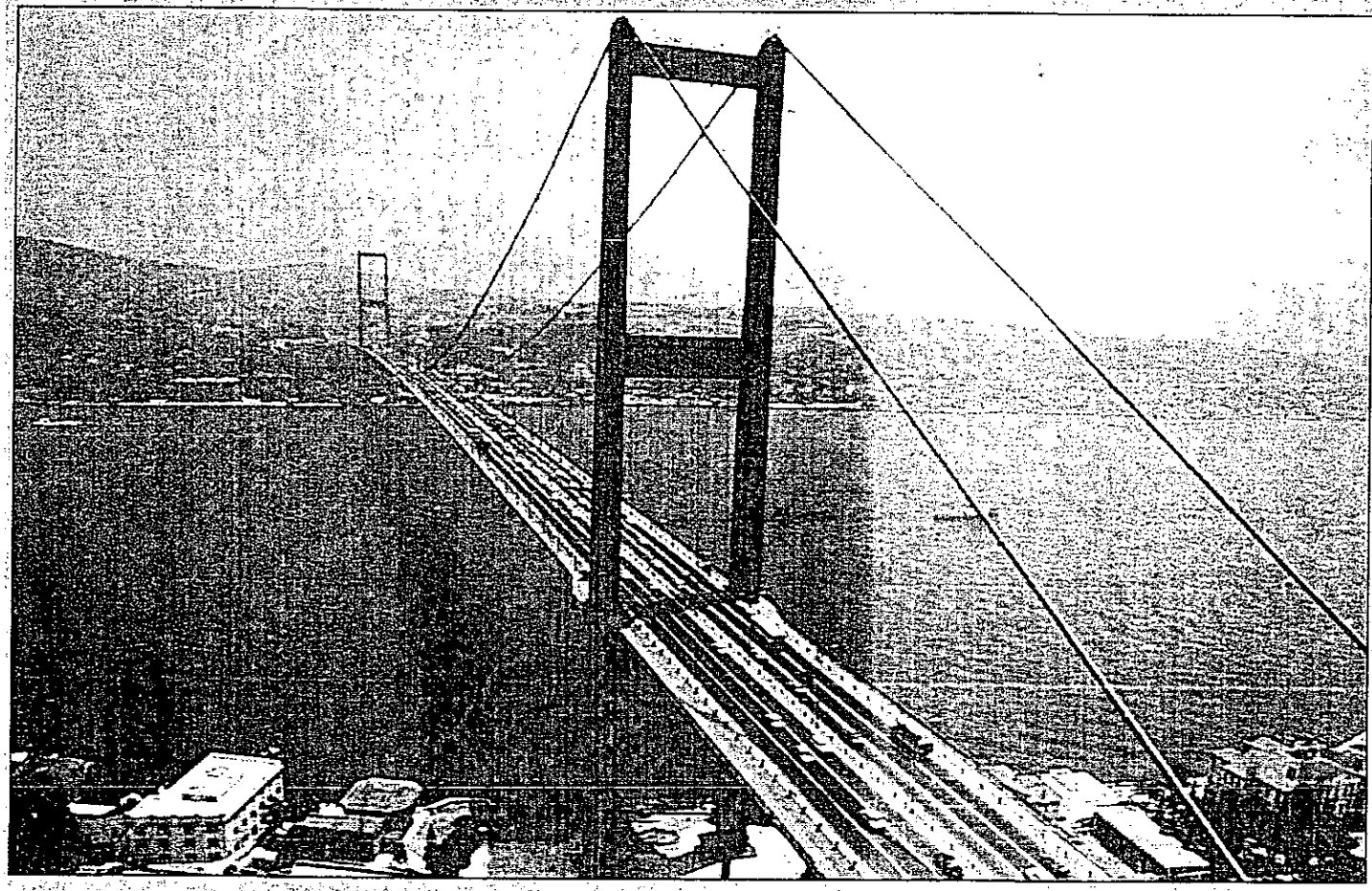


2nd Balkans and Middle East Countries Conference on Auditing and Accounting History

September 15 - 18, 2010 / Istanbul / Turkey

Conference Proceedings
Vol. III









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THE DEVELOPMENTS IN THE ACCOUNTING CULTURE AND FINANCIAL REPORTING IN TURKEY DURING THE REPUBLICAN ERA

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Abstract

In this study, previous studies that have been conducted relating to the "Uniform Accounting and Financial Reporting" in Turkey from 1923 to date was analysed within the historical process. Within this context first, financial reporting of the State Economic Enterprises (SEEs) and later regulations that formed the uniform accounting culture in Turkey are explained for the period between 1923 and 1950, and for the period between 1950 and 2000, respectively. Explanations for the companies that prepare different financial statements because of the sector in which they operate are presented. The Capital Market Board (CMB) regulations relating to the general chart of accounts and the financial statement formats are also explained for this period. Subsequently the period that began in 2000 was analysed. The Turkish economy suffered from high inflation over many years and this inflation gave rise to negative effects on financial reports. Moreover, unregistered economy is an important phenomenon for the Turkish economy. In the study, explanations for these factors that effect the financial reporting culture are presented. Furthermore, the Turkish Accounting Standards (TASs) that harmonized with the International Accounting Standards (IASs) are examined and thus an explanation on the Turkish accounting culture is provided.

Key Words: Uniform Accounting, Financial Reporting, The Capital Market Board.

1. Introduction

In the history of the Turkish Republic, founded in 1923, accounting applications were carried out in the form of adopting the quotations of western countries' accounting applications. During this period regulations relating to the field of tax formed the accounting applications in Turkey. As a result of this, a perception that the accounting records was made and financial statements were prepared for exercising the tax paying duty formed and this perception controlled accounting applications. Thus, accounting provided limited and inadequate information for users. On the other hand, the Uniform Accounting System (UAS) formed with statist understanding was applied in Turkey. The Uniform Chart of Accounts that is in the nature of an accounting framework came into force in 1994 as a mandatory application for all commercial and industrial companies. Moreover, different chart of accounts and financial statement formats were developed for some sectors that were based

on the nature of their activities. At the end of the 20th century, effective results were achieved consisting of accounting applications and audits through the formation of the UAS that formed the legal basis for the accounting profession. The aim of the study that is based on the literature review and review of regulations is to emphasize the transition process of accounting applications and financial reporting system from a tax oriented view point to true and fair information presentation view point.

In this study, the developments that effect financial reporting since 1923 is analysed within legal framework that existed up to 1950 and after 1950. The developments that occur after 2000 are explained with reference to the TASs. Moreover, in this study, explanations about the effects of inflation and the unregistered economy are presented.

2. Financial Reporting and Formation of the Uniform Accounting Culture Between 1923 and 1950

Before the proclamation of the Republic, Turkey had engaged in the Balkan War (1912-1913), World War I (1914-1918) and the War of Independence. The first 10 years of the Republic was a period in which our country, struggled for economic improvement and establishment of institutions, in which the basic political and governmental systems were established. The investment needs of our country were very high and the development of the Turkish economy was performed with nearly zero inflation. The rapid development that occured during this period was realized thanks to government assistance and public sector companies. Private sector companies, however, couldn't be activated. Because of these economic developments, the first accounting studies and applications were started for the SEEs. Our laws and regulations relating to the SEEs were generally formed by quoting from western countries' accounting rules and applications. At a later stage private sector companies started to grow and started to apply the accounting system and applications that were transferred from SEEs. Their accounting applications was formed by the Turkish Commercial Law (TCL) in 1937 and the tax reform in 1949.

The establishment date of the "Sanayi ve Maadin" Bank, ie. 1926, can regard as the starting point of accounting history in the Republican Era. The accounting organization of the four fabrics of the "Sanayi ve Maadin" Bank was developed by Professor Nihat Kiver. In 1933, the Sumerbank was found. To establishment the Sumerbank's accounting system, German Professor Sachsenberg was invited. The accounting organization that was established by him put new concepts on the accounting applications in Turkey. In the Sumerbank's accounting organization, types of cost, cost centers and cost allocation statements were applied. The chart of accounts included in the Sumerbank's accounting system was applied all the SEEs found later on.[1] Moreover this chart of account was a starting point to the development of private sector companies' accounting organizations. In this accounting organization Standard Cost System was formed. However this system was left because of the complications that occure correction entry in the end of period and Actual Cost System was used.[2]

Despite of the poor economic activity, the needs for recording, reporting and auditing of the financial statements occured in the first years of the Republic. To satisfy these needs, the Prime Ministry Supreme Audit Board was founded with 3460 numbered SEEs Law in 1938. Thereby an auditing organization different from the auditing organization of private sector

[1] Guvemli, Oktay, Türk Devletleri Muhasebe Tarihi,Cumhuriyet Dönemi XX.Yüzyıl (Accounting History of Turkish States ,Republic Era: XXth Century), Vol. 4, İstanbul: Avciol Publication; 2001,.2-8.,154-157.

[2] Erdogan, Avder, "Geçmişten Günümüze Muhasebe Mesleği" ("The Accounting Profession from the Past to Present"), 2007, www.muhasebetr.com (3.12.2009)

companies was found for the SEEs.[3] This organization was formed with quotations from the German Chart of Account and the German accounting rules. Our country's accounting applications was deeply affected by the TCL that became effective in 1937 and the Income Tax Law, the Corporation Tax Law and the Procedural Tax Law became effective in 1950. The TCL included provisions regarding joint stock companies beside commercial books that have to keep by entities. The joint stock companies part of the TCL was quotation from German Commercial Law. And literature of this period was founded on German resources. The adoption of the TCL had positively affect on the accounting applications.

The need for financing the government by income tax collected from taxpayers caused the emergence of the need for preparing and auditing the financial statements of private sector companies. To control the accounting records for the calculation of tax, the Ministry of Finance formed an expert team. Divisions such as the Supervisory Board of Finance, the Board of Tax Inspectors and the Board of Income Coordinators were established within the Ministry of Finance and persons that were experienced and qualified in accounting, financial reporting and auditing were employed by the government until the 1980's. The Tax Reform of 1949 was the biggest tax reform of the Republican Era. This reform was carried out by three important laws. These laws shaped accounting by affecting the documents and records organization, the balance sheets and the income statements. This tax reform was the starting point of the tax oriented accounting system in Turkey

3. The Accounting Culture, Financial Reporting and the Uniform Accounting System from 1950 to 2000

The accounting system of the SEEs rudimentary between 1940 and 1950 was developed with the efforts of the United States of America (USA) after 1950. With American experts arriving in Turkey and Turkish students going overseas for education in the USA, a close relationship began between Turkey and the USA. Turkey's accounting applications that had been influenced by the west previously; now began to be influenced by USA.

The planned development period that started in 1960 obligated both public and private sector companies to apply new accounting techniques.

In the second half of the 20th century, efforts to make legal arrangement for the accounting profession parallel with the tax laws developments form the UAS. During this period western European countries had a tendency to preserve monotype financial statements but apply different chart of accounts for different sectors. However, application of the general chart of accounts in Turkey was delayed.[4] The studies concerning the UAS can be grouped as follows:

a) The Uniform Chart of Accounts and the Financial Statement Formats in the State Economic Enterprises

More than half of their funds are received from the central or the local public administration and SEEs are audited by the central or the local public administration as well. In 1964, extensive regulations were made concerning the SEEs and a reorganisation committee was set up. The reorganisation committee dealt with developing the Uniform Chart of Accounts and the uniform financial statements, introducing the accounting terms and principles to the public. After some revision, the charts of accounts and financial

[3] Ekonomik ve Stratejik Araştırmalar Merkez Müdürlüğü ,Türkiye Ekonomisi -Tarihi Gelişimi, , Ankara: 2003: 10, (Center for Turkey's Ekonomic and Strategic Studies, Turkey Economy-Historical Development) http://www.kosgeb.gov.tr/yayinlar/duyuru.aspx?yID=105, (28.12.2009)

[4] Guvemli, op. cit. ..456-576

statements have came into use in 1972. A commission with the coordination of the State Planning Organisation was established in 1974, and made certain amendments on the UAS. At the beginning of 1977, the Uniform Cost Accounting came into use.[5] This chart of account was used by the SEEs until 1994, ie. until the general comminiqué on the "Application of Accounting System" was issued.

b) The Accounting Profession and the Uniform Accounting Ststem

The Turkish accounting culture has been affected by two important events: the admission of the accounting profession law and the formation of the UAS and the Uniform Financial Statements.

The required qualifications of people who are exercising the accounting profession and the works that will be done by them have been defined with Law No. 3568 of 1989 on "the Public Accountant, the Certified Public Accountant and the Chartered Accountant". Thanks to this Law, the accounting profession has attained a legal arrangement and the first step towards the formation of the accounting system in Turkey was made.[6] The professional titles, the required qualifications to assume these titles and the work that will be done by these people have been defined with this Law.

The second important step towards the development of an accounting culture was the formation of the UAS. The Ministry of Finance developed the accounting system and issued a communiqué concerning this accounting system, in 1992.[7] This communiqué which includes regulations on the fundamental concepts of accounting, the principles of financial statements, the preparation and presentation of financial statements, the UAS, the chart of accounts, and the working principles of accounts came into effect on January 1.1994. Thus, reliable accounting operations and the preperation and auditing of comparable financial statements were achieved for companies that keep their books according to the balance sheet. All the private and public sector companies were obligated to apply this communiqué's regulations. However, the companies, that keep their books according to the balance sheet but use different accounting techniques due to the features of the activity performed by them, such as the banks, assurance companies, special finance houses, leasing companies, mutual funds, securities investment trusts and financial intermediaries do not have an obligation to apply the UAS. However, these companies do have an obligation to comply with the fundamental concepts of accounting and the principles of financial statements. Different regulations were made concerning the chart of accounts that will be used by the said sector.

c) The General Chart of Accounts and Financial Statement Formats within the Framework of the Capital Market Board Regulations

After 1980, an important structural change occured in the Turkish economy with the transition to a free market economy, the liberalisation of exports and imports and the increase in the import of foreign capital. As a result of this change, the Capital Market Law (CML) was issued on July 30, 1981. The aim of this Law is to regulate and control the secure, transparent and stable functioning of the capital market and to protect and audit the rights and benefits of investors.[8] Within the scope of this Law, the Capital Market Board (CMB) was established in 1982 and the Board issued various communiqués to regulate the capital market.

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[5] State Planning Organization, , The Revision and Monotony of the Accounting Technics, Ankara: Ministry of Education Publication; 1973; 25

[6] Ministry of Finance, The Law Numbered 3568 , Official Gazette, 13.06. 1989

[7] Ministry of Finance, Comminiqué on the General Application of the Uniform Accounting System, Official Gazette, 26.12. 1992

[8] Capital Market Law, Official Gazete, 30.07. 1981, article.1

CMB Communiqués were classified by their subjects and issued as different Serials. From these Serials, Serial X includes the communiqués on "Independent Auditing" and Serial XI includes the communiques on "Accounting Standards". Communiqué Serial XI, No. 1 on the "Principles and Rules on Financial Statements and Reporting in Capital Markets" [9] was first issued in 1983 and then reissued in 1989 with amendments that cancelled the previous version. This Communiqué was the first step towards a uniform accounting for private sector companies and an important guide for accounting applications. In this Communiqué, the formats of the balance sheet, the income statement and the additional financial statement such as the cash flow statement and the fund flow statement were defined. Consequently, uniformity of the preparation of the private sector companies' financial statements was achieved. Moreover, generally accepted accounting principles were legislated for the first time with this communiqué. Furthermore, the necessity in the application of these principles to prepare the financial statements was emphasized. [10] The provisions that are in the second part of this communiqué, are related to the assessment of the financial statement items. These provisions focused on the profit calculation. Despite the fact that the TCL has no detailed regulations on valuation, this Communiqué includes detailed regulations regarding the basics of valuation whereby public companies are obligated to comply with these regulations. The provisions in this part are not related with the valuation principles and rules in tax legislation. Whether the books and documents kept by tax payers conform with the tax legislations or not are their own responsibility.

As a result of importation of foreign capital, foreign audit firms have begun to operate in Turkey. To carry out their audit function with specific standards, a need concerning a standard chart of accounts for the joint stock companies following CML took place. Thus, a chart of accounts was issued for the companies that were within the scope of this law and this chart of accounts was used until 1994 when it was replaced with the UAS by the Ministry of Finance in 1994 whereby all companies became obligated to apply this system.

Because of the features of the activities performed by intermediary corporations, the "Chart of Accounts for Intermediary Corporations and the Instructions for its Use" [11] was issued by the CMB. The intermediary corporations were obligated to comply with this chart of accounts. Moreover CMB, arranged a chart of accounts for mutual funds with the Communiqué on the "Principle and Rules on Mutual Funds' Financial Statements and Reports" because of the nature of the activities performed by these mutual funds. [12]

d) The Uniform Chart of Accounts and the Financial Statement of Banks and Insurance Companies

All legal regulations on banking involving provisions on the formats of the income statements and the requirements for the uniformity of these statements. The Banking Law No. 2999 which became effective in 1936 replaced the Law relating to protect of deposit dated 1933. Both laws included provisions on subjects such as the three year accounting abstracts, the format, the contents and the advertisement of the income statements. In the following years, this law was amended many times according to the requirements of the economy. The fifth version of the Banking Law was issued in 1985. The important feature of this law is the provision on the necessity of controlling the financial statements of banks by independent auditing organizations. The last decade of the 20th century was a failure for the Turkish banking system. The uncontrolled increase in the number of banks, the privatization

[9] Communiqué of Capital Market Board, Series: XI, Number: 1, Principles and Rules on Financial Statements and Reporting in Capital Markets, Official Gazete, 29.01. 1989

[10] Gucenme, Umit, Envanter (Inventory), Bursa, Alfa Aktuel Publication, 2002, p.17

[11] Communiqué of Capital Market Board, Series XI, Number 7, Official Gazette, 31.01.1992

[12] Communiqué of Capital Market Board, Series: XI, Number 6, Official Gazette, 28.02. 1990

of several banks and the banktrupcy of certain banks deeply affected economic life. As a result, the government made legal regulations continuously. The Banking Law No. 4389 which came into effect in 1999 was soon amended. Finally, the same law was reconsidered in May, 2001. With Law No. 4389 on "Organizing and Inspection Committee for Banks" was formed and with the formation of this well-equipped committee a new inspection organ was in charge. This Committee can make the decision to alienate the banks in dire straits to the Savings Deposit Insurance Fund, can demand again financial statements that it considers to be false statements, can remove the top management of banks and can restrain the operation of banks. Thanks to the "Bank Restructuring Program" begun in 1999, the Turkish banking sector has been built on firm ground to the present day. Today, Law no 5411 issued in Offical Gazette on Novenber 01, 2005 is still active in Turkey

The Uniform Chart of Accounts for the banks was prepared by the Banks Association of Turkey in 1986 as a necessity for transparent banking. Finally, the Banking Regulation and Supervision Agency published the regulations on the "Accounting Applications" in 2002 to harmonize with the IASs. [13]

Legal regulations concerning insurance companies started before the establishment of the Republic and the law numbered 1160 and dated 1927 was the first legal regulation of the Republic relating to insurance. The law on the "Supervision Of Insurance Companies" numbered 7397 and dated 1959 was being effective during the second half of the 20th century. That law achieved the formation of institutions relating to the insurance. In 1963 the "Insurance Supervision Committee" , which is stil active, was formed after the formation of the "Insurance Companies Union". In the law numbered 7397, there are regulations on the recording system , sending the balance sheets and the profit & loss statements to the concerning authorities and their advertisement, the ratios regarding the financial structure. With the amendment made later, the Uniform Chart of Account, which was prepared by the Union and approved by the "Undersecretariat of Treasury and Foreign Trade", was accepted to be applied. The Uniform Chart of Account applied by the insurance campanies at the end of the 20th century was prepared by the "Undersecretariat of Treasury and Foreign Trade" on May, 31st, 1995. According to this the financial statements including the balance sheets and the profit & loss statements were in three separate sets. So, separate statements for the insurance companies doing elementary business, separate statements for the insurance companies dealing with the life insurance and separate statements for the insurance companies doing both was setted.

The insurance companies applied the uniform chart of accounts that came into effect with the comminiqués dated 1993 fistly and after dated 2004 regard on the "Insurance Accounting System" and the "Insurance Chart of Accounts" [14] was issued by the Turkish Treasury. With the system became active in 2004, the accounting system of the insurance companies has now became parallel to the International Accounting System and the preparation of monotype financial statements has been achieved in the insurance sector.

[13] Banking Regulation and Supervision Agency, Regulation on Accounting Application, , Official Gazette, 22.06. 2002. This regulation revised by regulations that was issued in Official Gazete on October 23, 2002, November 29th , 2004 and June 30th 2005

[14] Communique on Accounting System of Insurance Companies and the Chart of Accounts for Insurance Companies, Official Gazette, 30.12. 2004

4. The Period After 2000: Financial Reporting According to the Accounting Standards in Turkey

In the eighth five-year development plan, including the years 2000-2005, the state drew itself back from production and introduced measures which let markets work in a more systematic and competitive environment. Starting from 2003 there have been some significant constructive improvements in the Turkish economy. These are the application of monetary policies to control chronic inflation, the decrease in nominal and real interest rates, the rapid growth of the economy parallel to a decline in inflation, political stability, and the increase in reliance on the Turkish economy. [15]

After 2000, studies concerning the formation of the TASs commenced and this process has carried on until today. The International Accounting Standards Committee (IASC), which has continued its activities since 1973, has published IASs in various subjects in order to abandon different accounting applications in different countries and to form an international accounting language. The Committee has revised the existing standards at certain periods. The Committee, has concentrated its studies on harmonizing the local accounting standards and developing the IASs, was reorganized in 2001 with a new name: The International Accounting Standards Board (IASB). The IASB has published the International Financial Reporting Standards (IFRSs) and these standards were applied by public companies in the European Union member countries.[16] In Turkey, certain regulations to harmonize with the IASs were made during the adaptation process to the EU regulations.

Firstly, the IASs was translated in Turkish in 1994 by the Turkish Accounting and Auditing Standards Board (TMUDESK) that was founded autonomously with the support of the Union of Chambers of Certified Public Accountants of Turkey (TURMOB). The Board published 20 national accounting standards and introduced them to the public.[17] These standarts have no sanction because they were not stated in any legal regulations. The standards concerning inflation and consolidation have appeared in the CMB Comminiqués' as compulsory that have to be applied by companies that followed the CML since 01.01.2003. Thus, the first regulations were made parallel to IFRSs. In 2003, the CMB, that has always been a leader in forming the accounting system in Turkey, published the comminiqué on the "Accounting Standards in the Capital Markets", which involved all IASs and which was the translation of the IASs.[18] This Comminiqué was the most significant step in the adaptation process of conforming to the IASs and for application of these standarts by the companies following the CML. This Comminiqué was abolished in 2008 and TASs was issued by Turkish Accounting Standards Board (TASB) that took this Communiqué's place.

On December 12, 1999 the TASB, was formed with financial and administrative autonomy and attached to the Prime Ministry with the addition of an article to the CML The reason for the Board's formation was to prevent the problems that resulted from the formation of different accounting standards in Turkey. This Board was established to form and issue the national accounting standards in Turkey and became active in 2002.

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[15] Ertuna, Ozer, "Türkiye Ekonomisinin Kayıp Yılları 1989-2002" ("The Lost Years of the Turkish Economy: 1989-2002") ,Mufad Muhasebe ve Finansman Dergisi, 2003; 17; 6

[16] A··dogan, Nalan, Muhasebe Standartlarına Genel Bakış: Uluslararası Finansal Raporlama Standartlarının İlk Kez Uygulanmasındaki İlkeler (General Survey on Accounting Standards: The Principles of the First Application of International Financial Reporting Standards), IX. Muhasebe Standartları Sempozyumu (IX Accounting Standards Symposium), Kıbrıs,2005; 8-11

[17] Turkish Accounting Standards 2000, Ankara, TÜRMOB Publication No. 95, 2000

[18] Communiqué of Capital Market Board, Series XI, Number 25, Accounting Standards in Capital Markets, Official Gazette, 15.11. 2003

The Board accepted the TASs published by TMUDESK as a draft in order to evaulate the studies done in the past and overview this draft before presenting it to the public. The TASs has been started to publish in the Official Gazette since January of 2005. At the present time, almost all of these standards were issued in the Official Gazette and revised. The studies on application of these standards by all companies including those that do not follow the CML is on-going. Within the globalization process, several countries such as Turkey and the European Union member states have made the necassary requirement to adapt the IASs because of the need to apply the same accounting standards between countries.

The application of the TASs resulted in certain changes in the formats and classification of the balance sheet, the income statement, and the cash flow statement that were determined by the UAS. In these standards, the importance of information was emphasized and fair presentation of this information was required. The TASs led to important changes concerning the valuation of the balance sheet and the income statement items. These changes have an important effect on the reported amounts in financial statements.

5. Factors that Effect the Financial Reporting Culture in Turkey: The Unregistered Economy and Inflation

The unregistered economy is the one of the most important problems in the Turkish economy and can be defined as all gainfull economic activities that can not be include in the Gross National Product (GNP) with the statistical methods that are used to calculate the GNP.

In the report of the Unregistered Economy Specialization Commission that was formed by the State Planning Organization in 2001 within the context of the eighth five-year development plan, the reasons, the results and the measures to prevent an unregistered economy was analysed. According to this report, the reasons for the unregistered economy were the development level of the country, the scarcity of institutional companies, the excess amount of small- and medium-sized enterprises, the high inflation, the severe and inequable taxation system, the complexity of tax legislation and the ineffective tax audits. During this period, studies to prevent an unregistered economy and to register them were done and regulations on inflation adjustment were made.

The Tax Procedure Law was amended in 2003. According to this Law, income and corporation tax payers who keep their books according to a balance sheet, will adjust their financial statements according to the inflation adjustment at the end of the temporary tax period if the requirements that specified in the Law exist. Moreover, in the year 2003 inflation adjustment was applied to the financial statements of the companies without any condition on them. Inflation adjustment can be defined as converting the Turkish lira amount of the financial statement items to the amount in the financial statements' presentation date. The aim of the inflation adjustment in Turkey was to end the negative affects of high inflation that occured in financial statements over many years and to provide fairl taxation by gathering taxes on the real income of tax payers and in this way reduce the avoidance of tax both the actual and potantially. However, because the government followed inflation preventive politics in succeeding years, conditions specified in the Law did not come to fruition and inflation adjustment was not applied.

6. Conclusion

In Turkey, accounting was formerly used as a means of getting information from public corporations, and later, accounting began to cover private corporations as a result of the development in commerce. The provision of the Income Tax Law, the Corporate Tax Law

and the Tax Procedure Law which became effective with the Tax Reform of 1949 affected the accounting system and became a starting point for tax oriented accounting view point in Turkey. With the TCL, the CML and regulations on the UAS, concepts such as commercial profits and accounting for information became important. The Accounting Profession Law and legal regulations on independent audit were important steps made towards the formation of an accounting system and preperation of true and fair financial statements. In the process of globalization, the European Union countries and countries including Turkey have made the necassary requirements to adapt to the IASs since 2005. The development and application process of the TASs harmonized with the IASs still continues in Turkey.

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