



## The origins of modern accounting in Brazil: Influences leading to the adoption of IFRS

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### ABSTRACT

Despite the increasing importance of Brazil, there has been little documentation of how accounting developed and about the significant formative influences involved. This paper explores the significant influences on Brazilian accounting and the path to the adoption of International Financial Reporting Standards (IFRS). Several important influences are emphasized: the equity theory of the Italian school of accounting in the early 20th century; the birth of the Brazilian accounting profession in 1931 and the certified accountants association in 1946; the impact of US trade and American accounting in the 1950s; and the high rates of inflation that occurred from the beginning of the 1960s. Modern Brazilian accounting had its beginning in the 1970s with the development of the stock market, the reforms of the financial system, and the decrease of tax influences on accounting. The globalization process and the need for Brazilian accounting to converge with international accounting led to the decision to adopt IFRS in 2007.

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### Introduction

Brazil is one of the fastest growing emerging economies in the world. It is expected to overtake both Britain and France by 2050 and move into fourth place in the ranking of world economies (PWC, 2011). As one of the BRIC countries (the media shorthand of Brazil, Russia, India and China), Brazil is an increasingly important player in the world economic stage – as evidenced by its recent membership to the G-20. Until the early 1990s, it was seen as an economy which had huge assets but which lacked the structure to provide long-term success. Inflation had long been out of control but the measures taken in the 1990s have overcome these difficulties.

In this environment of economic stability and with inflation under control, there was a major change in the Brazilian capital markets with strong institutional develop-

ment and rules to improve corporate governance. To support the development of capital markets, the decision was made to move away from a domestic to a global financial reporting system. The gradual convergence of Brazilian accounting rules with International Financial Reporting Standards (IFRS) began in 2006 for financial intermediaries under the supervision of the Central Bank and in 2008 for public companies with a deadline of 2010 for full convergence. In January, 2010, a Memorandum of Understanding was signed between the relevant Brazilian accounting bodies and the International Accounting Standards Board (IASB) which confirmed the end of 2010 as the target date for full convergence.<sup>2</sup>

Despite the increasing importance of Brazil, there has been little documentation of how accounting developed and about the significant formative influences involved. This paper seeks to portray the development of accounting in Brazil, namely the significant influences which occurred in the 20th century and the path to IFRS adoption. It is

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<sup>2</sup> <http://www.iasb.org/NR/rdonlyres/B7F3624B-1DFF-4E96-BFF0-BF74D1C650B/0/MoUBrazil.pdf>, accessed March 15, 2011.

organized as follows. “The significant influences leading to the modern Brazilian accounting” section identifies the main drivers of accounting development: in the early years of the 20th century, the influence of the equity theory of the Italian school of accounting on the Brazilian accounting; the birth of the modern accounting profession in 1931 and the formation in 1946 of the certified accountants association (*Conselho Federal de Contabilidade*); the change in accounting thought in the 1950s as a consequence of trade with the USA; the high rates of inflation that occurred from the beginning of the 1960s that led to Brazilian contributions to inflation accounting methods. “Brazilian accounting in the modern area” section explores Brazil’s modern accounting which has its beginning in the 1970s, with the development of the stock market, and the reforms of the financial system. In this period there was a decrease of tax influence on accounting and an increased influence of the American school of accounting. In 2005, the globalization process and the need for Brazilian accounting practices to converge with international accounting led to the decision to adopt the International Reporting Financial Standards (IFRS) issued by the International Accounting Standards Board (IASB). In the last section of the paper, the main conclusions of the study are presented.

### **The significant influences leading to the modern Brazilian accounting**

#### *The Italian influence on Brazilian accounting thought*

At the end of the 19th century, there was a need to introduce bookkeeping for business management associated with strong economic development that was taking place in São Paulo, especially as a consequence of the expansion of the coffee industry and its multiplier effect on urban activities. New schools were created that offered an accounting degree that certified accounting professionals: in 1894, the Polytechnic School of São Paulo and in 1902 the Practical School of Commerce (Rodrigues, Schmidt, Fonseca, & Santos, 2011). In this new academic context, Francisco D’Áuria (1884–1958) was responsible for the introduction of the Italian accounting thought in Brazil. In 1912, the first edition of the *Revista Brasileira de Contabilidade* (Brazilian Review of Accounting) was published (in June 1922, replaced by the *Revista Paulista de Contabilidade* (Paulista Magazine of Accounting)). This Journal was inspired by the Italian Journal of Accounting and was an initiative of Horace Berlinck, Carlos Carvalho Costa Sampaio and Francisco D’Áuria (Sá, 2008). At that time, Brazilian accounting was influenced by Italian equity theorists for whom accounting was not just a professional area that aims to give the fair and true value of assets and liabilities, but a science, with its own laws and principles, and an objective to study and interpret net assets. The focus of the equity theory of the Italian school was doctrinal and theoretical. Additionally, in this period several accounting bodies were created (Ricardino, 2000). They were important in starting an organized accountancy profession. In 1921, the *Instituto Paulista de Contabilidade* (Paulista Institute of Accounting) and the *Instituto*

*Brasileiro de Contabilidade* (Brazilian Institute of Accounting) were founded in S. Paulo and Rio de Janeiro, respectively. In 1924, the first Brazilian accounting congress was held in Rio de Janeiro, and the main topic was the professionalization of accounting (De Rocchi, 2007).

In June 26, 1926, through decree 17390, known as the Souza Reis Regulation, a new income tax regulation was approved. It is considered to have been the most important event in the history of income tax in Brazil and was in force for the longest period, until its replacement in 1976. It also marked the first step in the process of tax legislation impacting accounting practices in Brazil (Assis, 1998, p. 30), another influence of European or Continental accounting in which accounting rules are tax-influenced and law-based (Nobes & Parker, 2004).

#### *Corporatism and the birth of the modern accounting profession in Brazil*

The Brazilian Revolution of 1930 brought Getúlio Vargas to power. He ruled Brazil until 1945, first as provisional president (1930–1934), then as constitutionally elected president (1934–1937) and finally, as dictator of the pseudo-fascist New State (*Estado Novo*) (1937–1945) (Bak, 1983, p. 255). Vargas returned to power in 1951, when he started a new term of 3 years.

The “corporatist”<sup>3</sup> President Vargas considered it a responsibility of the new regime to join elements of labor and production, and to coordinate through the government the training of accounting technicians for Brazil that “we so badly need” (Vargas, 1938, p. 106). The commitment of Vargas to industrialization and import replacement created an impetus to the development of accounting. More accomplished accountants were also needed to help the Federal Government supervise tax collection. It was therefore considered necessary to regulate the accounting profession. This happened in July 9, 1931 through the publication of decree 20158 in the *Diário Oficial da União* (Official Journal of the Federal Administration) (which also reformed technical commercial studies). The government issued professional regulations that provided the framework for the establishment and monitoring of a certified accounting profession. To become a certified accountant it was necessary to have graduated from an authorized school with a diploma validated by the *Superintendência do Ensino Comercial* (Superintendent of Commercial Education) (Title III of decree 20158). The professional practice of accountants was subsequently regulated by a network of professionally-sponsored Federal and Regional Councils of Accounting created in 1946.

Awareness of the need to generate reliable accounting information emerged. In the 1930s, the Vargas

<sup>3</sup> “Corporatism can be defined as a system of interest representation in which the constituent units are organized into a limited number of singular, non-competitive, hierarchically ordered and functionally differentiated categories, recognized and licensed (if not created) by the State and granted a deliberate representational monopoly within their respective categories in exchange for observing certain controls on their selection of leaders and articulation of demand supports”. (Schmitter (1974), cited by Lloyd-Jones, 1994, p. 8). As Rodrigues, Gomes, and Craig (2003) argue corporatism and neo-corporatism regimes support the regulation of professions.

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