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Intellectual Capital and Management Accounting Practices: Evidence from Iran

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Abstract

The purpose of this paper is to propose a framework to investigate the association between the level intellectual capital (IC) and management accounting practices (MAPs) within the Iranian public listed companies. In particular, it aims to examine whether companies with higher level of IC are more likely to place importance on more contemporary management accounting (MA) approaches. The premise of "fit as mediation" of contingency theory is borrowed to explore the potential association between the level of IC and the use of specific MA perspectives in terms of performance measurement and budgetary control techniques. This model brings more useful insight in linking IC to MAPs and those techniques which tend towards strategic-oriented approaches within Iranian context, thereby suggesting that some evolution in MAPs stems from focusing too intently on IC and intangibles. The Iranian public listed companies from Tehran Stock Exchange (TSE) are selected as the ideal setting to examine the relationship between IC and MAPs since most of them are medium to large-sized companies that plausibly enjoy greater resource available for investment in knowledge-based resources and also actively engaged in more innovative and strategic MAPs. This study provides insights into the way practitioners and organizations adopt appropriate MA approaches, to be aligned with the level of IC in a company, with the ultimate purpose of taking full advantage of those knowledge related resources.

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Keywords: Intellectual capital; Management accounting; Tehran Stock Exchange (TSE); Iran

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1. Introduction

Globally, information-age economy has superseded the industrial and retail economy (Canibano et al., 2000). Davenport and Prusak, (1998) argued that knowledge and information play a leading part in today's rapidly changing environment where pioneer businesses are incrementally knowledge-intensive and technological driven. The traditional financial statements and management accounting tools are not efficient any longer in today's knowledge-intensive environment where organizations depend heavily on knowledge capabilities and intellectual capital (IC) for success (Huang et al., 2010). These intangible assets and resources are perceived as the cornerstone of gaining competitive advantage for the knowledge firms. In essence, IC reflects all the precious and inimitable capitals which are inevitable for value creation of a company (Roos et al., 2005; Johannessen et al., 2005; Marr et al., 2004; Roos et al., 2001; Nahapiet and Ghoshal, 1998; Bontis, 1998; Roos and Roos, 1997; Sveiby, 1997).

Growing demands are being placed on management accounting to detection, measure and disclose IC value and performance in parallel with the awareness of executives concerning the important role of intangibles in engendering profitable business (Marr and Chatzkel, 2004). According to Edvinsson and Sullivan (1996), knowledge management needs knowledge measurement where knowledge-intensive companies reap their profits from innovativeness and knowledge-based practices. Although the main focus is on external reporting, IC literature in accounting tends to be diverse (e.g. Bukh et al., 2001; Guthrie, 2000 and Mouritsen et al., 2001a). Limited information on intangibles is provided through external financial reports (Financial Accounting Standards Board, 2001; Wallman, 1995). According to Eccles et al. (2001), capital markets need more robust and reliable information in relation to firm knowledge capabilities such as strategic priorities, risk elements, know-how, integrity and management qualities and this can be provided by IC information offered via private channels like presentations to analysts (Holland, 2003; Garcia-Meca et al., 2005).

Accordingly, the value drivers should be determined, measured, and provided by managers in order to develop information system, performance measures and resource allocation for shareholders (Ittner and Larcker, 1998). This implies that firms with high levels of IC must possess advanced management accounting and control systems (MACS) which support such efforts. From theoretical lens, disclosure of value content information on intangible bring about transaction cost and uncertainty reduction which in turn leads to mitigation of adverse selection problems regarding voluntary disclosures and investors(Diamond and Verrechia, 1991; Lev, 1992; Botosan, 1997; Healey et al., 1999; Leuz and Verrechia, 2000). Hence, these seem so similar to agency approach employ in the organization. MACSs are required to be developed in order to cope with these problems. Nevertheless, there arelimited empirical endeavors directly on how the IC have made a major breakthrough in the emergence of contemporary MACSs and practitioner-oriented literature has become cliché (Roslender and Fincham, 2001).

This study primarily aims to link IC to management accounting practices (MAPs) and those techniques which tend towards strategic-oriented approaches. In other words, it investigates whether, and if so, how companies with great level of IC have evolved their MAPs to deal with the matter that accounting for IC promotes. As Tayles et al., (2002, 2007) discussed, such organizations plausibly tend toward a more strategic MAPs and concentrate on the evaluation and measurement of IC to avoid overlooking the firm's most precious assets. Nevertheless, there is limited insight into how MA plays a role in managing IC within knowledge-based organizations. The study, therefore, investigates how MAPs develop as companies reconcile their strategic plans and functions to reflect the developing knowledge-based economy.

The paper is structured as follows. In the subsequent sections, literature review and hypotheses development are presented followed by a theoretical framework which explains the relationship between IC and MA.

2. Literature Review

2.1. Intellectual Capital

Broadly speaking, intellectual capital has aroused considerable interests in the recent years. From two previous decades a plethora of studies have placed too much value on IC as an important driver and indicator of national and international economic development (Sveiby, 1997; World Bank, 1998, Cabrita and Vaz, 2006). It has also provided