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The Westernisation of a financial reporting enforcement system in an emerging economy

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Building on semi-structured interviews and publicly available documents in the realm of accounting, auditing and capital market regulation in Romania, this paper reviews and reflects on the prerequisites for, and conditions affecting the development of a financial reporting enforcement system (FRES) of Western origin in an emerging economy. It does so by examining institutional factors within and across the key components of the Romanian FRES, namely the engagement of the preparers and auditors of corporate financial reports and their interactions with public oversight bodies. The creation and functioning of the Romanian FRES are driven by the dynamics between Western and local pushes and pulls. Western actors offered support, especially in terms of technical assistance and educational programmes, but the Romanian government delayed the implementation of local support mechanisms, such that practices and mindsets did not change initially. Although practices and institutions have evolved since the country joined the European Union in 2007, the pursuit of a functional Western-based FRES remains an on-going process that is highly dependent on both the continuous external provision of adequate resources and the enrolment of national actors in the deployment of these resources.

Keywords: institutional change; Romania; IFRS; enforcement

1. Introduction

Transitional and emerging economies have witnessed ‘an ideological U-turn’, which has resulted in the adoption of an ‘all-market mantra and radical forms of political and/or cultural liberalism’ (Djelic 2006, p. 67). Western institutions of accounting and auditing—such as International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards

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Board (IASB) and related oversight and enforcement mechanisms—are claimed to promote a market ideology and spread a Western type of capitalism (Arnold 2012). Whenever such institutions meet emerging contexts, tensions can occur (Cooper & Robson 2006, Suddaby et al. 2007). These tensions are often explained by a ‘balance of local institutional pulls and foreign institutional pushes’ (Soulsby & Clark 2007, p. 1430).

This was very much the case following the collapse of the Soviet Bloc, when many of its former member states had ‘the desire to belong to the West’ (Mennicken 2008, p. 388). They willingly embraced the arrival of Western organisations, such as the World Bank (WB) and the International Monetary Fund (IMF), and the accompanying economic and regulatory doctrines. Studies of former socialist countries adopting Western accounting and auditing standards have identified a variety of institutional difficulties within this process. For example, King et al. (2001), Samsonova-Taddei (2013), and Albu et al. (2014) found that old accounting practices persist even though national regulatory frameworks have been aligned with Western standards. Mennicken (2008, 2010) and Samsonova-Taddei (2013) emphasised the significance of social structures and established networks of national actors in preserving and reproducing existing accounting practices, independent of regulatory changes. Sucher and Jindrichovska (2004) and Vellam (2004) suggested that some of this is because financial reporting information retains a different status in transitional and emerging economies. Such information continues to be primarily regarded as useful for taxation and state control, rather than to inform investors or markets (Apostol & Pop 2019).

This paper studies how a Western type of Financial Reporting Enforcement System (FRES) was created and duly evolved in post-socialist Romania, after the fall of the Ceauşescu administration in December 1989. Financial reporting enforcement is about ‘examining the compliance of financial information with the relevant financial reporting framework, [and] taking appropriate measures where infringements are discovered’ (ESMA 2014, p. 38). It is an integral part of a country’s accounting system, and typically comprises three core elements, namely company control systems and management practices dedicated to financial reporting; independent auditors as experts in the rules, standards, and regulations; and public oversight mechanisms (FEE 2001, Brown & Tarca 2005).

Following the WB’s and the IMF’s recommendations, and with a vivid desire to join the European Union (EU), Romania embraced swift changes to its legislation after 1989 and, with a view to turning into a market-based economy, also adopted Western modes of accounting regulation. Nonetheless, the Romanian environment has been characterised as highly unfavourable to the adoption of related frameworks (Albu et al. 2014, Brown et al. 2014), because, under Ceausescu’s regime, accounting had been exclusively shaped by, and performed for, the socialist state apparatus (Calu 2005). A rules-based and technocratic approach, all-encompassing secrecy, an emphasis on taxation, and a focus on state-centred monitoring and control were characteristic of the country’s institutional environment.

With the *Fédération des Experts Comptables Européens* (FEE – Federation of European Accountants) noting that financial reporting enforcement takes place in, and depends on, the institutional environment in which it operates, this study gives particular attention to the institutional features that FEE (2001) identified as most significant to the establishment of a Western-type FRES in an emerging context. The study draws on publicly available documents and proceedings in the realm of financial reporting enforcement, in particular accounting, auditing and capital market regulation in Romania, as well as semi-structured interviews with individuals with extensive working experience who are or were involved in the creation and/or operation of the Romanian FRES.

The paper seeks to make three contributions. First, it offers a case study of the Westernisation of emerging economies (Arnold 2012), exploring how Western norms and principles make their

way into a non-Western context, and discussing the restrictions on, and possibilities of, local action. As such, this rich descriptive study of an individual jurisdiction (Camfferman & Zeff 2018) is a direct response to calls ‘for an enhanced focus on the influence of national political and social contexts on the development and interpretation of accounting regulations’ (Canning & O’Dwyer 2013, p. 169) and how ‘historically-rooted modes of regulation [...] [relate] to the efficacy of emerging oversight institutions’ (Caramanis et al. 2015, p. 28). In Romania, the national political agenda generated an initially enthusiastic embracing of Western frameworks, but the government failed to nurture the supporting mechanisms that are essential to facilitate the implementation of related norms, values, and mindsets. The training and education of national actors and the creation of incentive systems for them to engage with the new doctrines were not prioritised. In consequence, initially, formal checks of the timely filing of financial statements were the sole enforcement measure. Only gradually, and in response to continuous demands by Western actors such as the WB, the IMF, the EU, and foreign investors, were these amended to include elements of Western origin, for instance substantial checks on whether the filed statements actually complied with the relevant financial reporting framework. The paper’s analysis suggests that the development of Western enforcement practices over more than 25 years has set a good ground for a further integration of the country and its FRES into the Western world. Nonetheless, the slow pace of this journey mirrors the overall difficulties in reforming a country’s entire accounting system.

Second, by developing an in-depth understanding of the role of national enforcement, this paper informs the IFRS adoption literature (e.g. Brown & Tarca 2005, Daske et al. 2013, Cascino & Gassen 2015, Ball 2016, De George et al. 2016). Many studies in this literature have employed selected elements of a country’s legal system, such as the ‘rule of law’, ‘regulatory quality’, and the ‘strength of the capital market’ (La Porta et al. 1998, Kaufmann et al. 2010), to measure levels and degrees of national enforcement. These proxies, however, do have limits in terms of their ability to capture the whole enforcement process associated with accounting (Brown et al. 2014). Our study complements this stream of literature by highlighting the significance of institutional forces, such as the presence and engagement of Western actors in transitional contexts, and their role in the effective functioning of an enforcement system. For the specific case of Romania, we found that the national auditors and public oversight bodies ended up embracing a staggered approach to implementing enforcement norms. Western actors pushed towards the adoption of their own standards, such that, on the surface, the local norms appeared to be fully aligned with Western frameworks. However, the resulting enforcement practices have continued to draw on elements of local origin. This was explicitly the case in the 1990s when old practices were maintained even under the new standards, laws and codes. By the 2010s, practices were more consistent with Western modes of enforcement, albeit still flavoured with, and characterised by, local interpretations and adaptations.

Third, through mobilising the case of a post-socialist country that faced drastic institutional reforms, this paper speaks to broader debates on the complex dynamics associated with processes of institutional change (Thornton et al. 2012, Kern et al. 2018). Prior studies on post-socialist contexts have acknowledged that such transformation processes tend to reflect the influences of various factors and actors (Child & Czeglédy 1996, Soulsby & Clark 2007). Our analysis suggests that the creation and operation of the Romanian FRES has been shaped by the country’s political and historical legacy, and the manifold interactions and negotiations between Western and Romanian actors. In resource environments characterised by weak incentives for national actors to unlearn the past and change established practices, the creation of new institutions can be particularly critical and this, in turn, would appear to depend highly on Western actors providing a continuous supply of resources. However, it also matters considerably how resources are used by the national actors, especially in terms of seeking to align the behaviour and perspectives of key

Western and national actors. In emerging economies, change can be a discontinuous and lengthy process of adoption and transformation. Using foreign resources to implement educational initiatives and provide regulatory advice, technical assistance, and monetary incentives can be very helpful in facilitating institutional change, especially if national actors are involved in their deployment and work to tailor measures to the specific needs of the local context.

The remainder of the paper is organised as follows. Section 2 provides the contextual background on the FRES in Romania and details how this system has been westernised after 1989. Section 3 presents the study's research approach. The case narrative analyses the dynamics and critical institutional factors in Romania's adoption of a Western FRES along three key processes within a FRES, namely corporate self-enforcement (section 4), auditing (section 5), and public oversight (section 6). The final section discusses our findings and concludes the paper.

2. Background to Romania's financial reporting enforcement system and its Westernisation

During Romania's socialist regime (1947–1989), accounting served the needs of the central government in managing and planning the entire economy. Accounting information was exclusively prepared for the state, and public disclosure was non-existent (Calu 2005). As the main purpose of accounting was to create a data pool for the state, its significance was reduced to bookkeeping, which is why the keeping of proper accounting records and documentation was much more important than preparing any type of financial statements (Parker 2008b). Similar to other Soviet Bloc countries, accountants were state servants who operated accounting 'instruments to facilitate the realisation of socialism' (Mennicken 2010, p. 334).

After the fall of the socialist regime in December 1989, Romania swiftly aimed to make the transition from a centrally planned to a market economy. Desiring to become a member of the EU, the country introduced a number of significant economic reforms, including the privatisation of state-owned companies, initiatives to enhance competition, as well as measures to promote capital inflows and create opportunities for foreign direct investments (see, e.g. King et al. 2001, Roaf et al. 2014). These reforms were supported by funds and advice from Western organisations, such as the WB, the IMF, the EU, and the European Bank for Reconstruction and Development, as well as individual countries, such as France and the United Kingdom (Child & Czeglédy 1996, Delesalle & Delesalle 2000, Roaf et al. 2014).

Due to their previous economic, political, and social relationship, bilateral agreements between Romania and France significantly influenced the initial post-socialist accounting reforms. A French team of experts helped in drafting the 1990 Companies Act and the 1991 Accounting Act (Delesalle & Delesalle 2000). Aiming to instil the ideas of separating management from financial accounting and making corporate financial data publicly available, the new legislation mandated the preparation of financial statements based on codified accounting and measurement principles (King et al. 2001). This new accounting regime provided the institutional infrastructure for the creation of a capital market, such that, in 1994, the *Comisia Națională a Valorilor Mobiliare* (CNVM – National Securities Commission) was duly created as the supervising authority for the revived *Bursa de Valori București* (BVB – Bucharest Stock Exchange).¹ In 1996, under a bilateral agreement with the United Kingdom, the British government's Know How Fund² became involved. It initiated a project with the Romanian Ministry of

¹BVB had originally been created in 1882 but was shut down by the socialist regime in 1948.

²This fund was set up by the British government, to assist those countries that were part of the Soviet Bloc in transitioning towards market economies.

Public Finances, establishing an expert group to discuss how to amend accounting, auditing, and financial reporting enforcement standards, norms, and institutions to make them more suitable for a market economy (Delesalle & Delesalle 2000).

Facing severe economic difficulties in the mid-1990s, Romania contracted financial support from the IMF and the WB. In return for their support, further structural reforms were demanded at the macroeconomic level, such as accelerated privatisation and financial sector improvements, including capital market regulatory frameworks. In turn, the WB and the IMF, both supporters of International Accounting Standards (IAS), 'indicated the direction to be taken by accounting in Romania in order to secure World Bank and IMF loan facilities' (King et al. 2001, p. 158). This push eventually led the expert group established by the British to recommend that Romania consider the adoption of IAS. Subsequently, in 1999, with the exception of the standards relating to consolidation and hyperinflation, IAS were included in the national accounting regulations applicable to all large companies in Romania. This was also the year when Romania adopted International Standards on Auditing (ISAs), and when Western organisations and institutions recognised the country for its regulatory improvements (King et al. 2001).

In parallel with engaging with the WB and IMF, the EU's regulatory agenda also became institutionally relevant for Romania. In aspiring and preparing for membership, Romania had to align its legislation with prevalent EU law. In 2000, the EU's Financial Service Action Plan triggered a shift towards a more stringent capital market discipline in all member states. As an immediate consequence, an expert group drafted a concept report for an integrated European capital market (Lamfalussy et al. 2001). It concluded that all EU capital market-oriented companies should apply the same accounting standards, and subsequently the EU mandated all listed companies to prepare their consolidated financial statements in accordance with IFRS, subject to endorsement through the EU's IFRS comitology procedure. The report also pointed out that a harmonised enforcement system for IFRS compliance would be required for the capital market to work properly, acknowledging that the successful adoption of international accounting and auditing standards depends on enhanced compliance and enforcement (Lamfalussy et al. 2001, p. 40). Thus, the 2004 Transparency Directive (2004/109/EC) required EU member states to implement national measures and systems for the correct application of IFRS. The (non-binding) Committee of European Securities Regulators³ (CESR) Standards No. 1 and No. 2 laid the foundation for the modelling of a FRES in all member states (CESR 2003, 2004). Though these guidelines are still not ultimately binding for the individual EU member states and their financial market supervisory bodies, national authorities 'shall make every effort to comply with those' (Article 16 (3) ESMA Regulation), and most EU jurisdictions had already followed these recommendations by 2008 (CESR 2009).

In the final preparations of joining the EU in 2007, Romania eventually amended its capital market regulations in line with European requirements, such that CESR (2009) classified Romania as partially implementing the principles included in CESR Standard No. 1, with only 2 out of the 21 principles not being followed. Despite this apparently high level of formal compliance with EU enforcement requirements, in practice significant discrepancies between Romania and Western Europe remained (WB 2008, Brown et al. 2014). Emphasising that the Romanian FRES was still deficient amongst its EU peers, ESMA concluded that:

some fundamental problems with enforcement needed to be corrected before it could be said there is an effective enforcement of financial information in Romania. (2017, p. 21)

³In 2011 the CESR was superseded by the ESMA, and, in 2014, the CESR standards were replaced by the 'ESMA Guidelines on enforcement of financial information' (ESMA 2014).

The Romanian developments feature in a wider context. During the 1990s, the global impact of local financial crises in emerging economies and regions around the world, such as in Mexico (1994/95) and Asia (1997), raised worldwide concerns regarding global financial stability. These crises triggered the ‘new international financial architecture’, which proposed the global endorsement of a system of international standards for accounting, auditing, corporate governance, and capital market supervision (Humphrey et al. 2009).

Through their various programmes and measures that aim to provide financial aid and expertise to emerging economies, the WB and the IMF have contributed to the global diffusion of these standards (Arnold 2012). This is foremost because the financial assistance these organisations provide is conditional on the country’s commitment to implementing economic and institutional reforms according to international standards (IMF 2017).⁴ The neo-liberal doctrine promoted by the WB and the IMF posits that copying Western macro-economic rules would swiftly change the conduct of actors in emerging sites (Soulsby & Clark 2007). This view, however, oversimplifies the institutional complexities and interdependencies accompanying the transformation from a socialist to a capitalist economy, and disregards the limited capabilities available in many emerging sites to assimilate Western practices. Indicative of the practical struggles that many former socialist countries in the Central and Eastern European (CEE) region have faced when creating FRESs in the context of becoming market economies, Deacon et al. (2007, p. 236) cautioned that ‘empty institutions have been created [...], EU-like legal frameworks downloaded, cut, and pasted, but with little real institutional follow-through’.

The following section introduces the research approach we deployed for the detailed analysis of the impact national and Western actors had on the creation of a FRES and related institutional change in Romania after 1989.

3. Research approach

A country’s institutional environment in terms of accounting and auditing is characterised by the relevant parts of the jurisdiction’s legislative framework, its accounting profession, accounting education and training, the processes for setting accounting and auditing standards, and the arrangements for ensuring compliance with applicable norms, rules, and other regulations (IMF 2017).⁵ It is, therefore, not surprising to find Camfferman and Zeff (2018) observe that the worldwide implementation of IFRS, related international auditing standards, and enforcement oversight bodies, all modelled along Western ideals, created tensions in some jurisdictions. The countries in the CEE region, such as Romania, are among those jurisdictions where tensions are particularly distinct, and where institutional change has often been ‘accompanied by local resistance, exceptions, and mutations’ (Mennicken 2010, p. 335).

Prior studies of the CEE region have highlighted the significance of national culture, the communist legacy, dense and specialised networks of actors, and the complex relationships between the heterogeneity of laws and regulations as critical institutional factors shaping the accounting and auditing environments (e.g. King et al. 2001, Sucher & Jindrichovska 2004, Vellam 2004,

⁴These organisations provide financial aid and expertise to emerging economies to implement standards and codes that are expected to contribute to macro-financial stability and crises prevention (IMF 2017). In this context, they also monitor the implementation progress of the agreed international norms. For example, in the 1990s the WB and the IMF launched their Standards and Codes Initiative, and since then have issued Reports on the Observance of Standards and Codes (ROSC), which also cover accounting and auditing standards.

⁵The WB and IMF also review these components when they survey national systems and their compliance with the agreed international norms.

Mennicken 2008, 2010, Samsonova-Taddei 2013, Albu et al. 2014). These factors can hence be expected to influence how Western standards and frameworks are turned into national accounting, auditing, and enforcement practices. It has also been suggested that legal correctness, internal orientation, and a rules-based approach to regulation, all relics from Soviet times, continue to influence significantly the business and resource environments of such economies (Kriauciunas & Kale 2006, Tilcsik 2010). These features have been identified as a fundamental part of Romanian culture (Calu 2005) and could be expected to enable and constrain various actors' and institutions' ability and willingness to engage in enforcement practices (Parker 2008a). This is why it was decided to mobilise an institutional analysis for assessing the relative commitment of national and Western actors to fundamental institutional change in the process of establishing a FRES in Romania.

A FRES, in the Western sense, has been said to comprise typically three core elements, namely company control systems and management practices dedicated to financial reporting; independent auditors as experts in the rules, standards, and regulations; and public oversight mechanisms (FEE 2001, Brown & Tarca 2005). It has also been claimed that the effective creation of a FRES requires all of these three key elements to 'work efficiently: the system will be as strong as its weakest part in delivering strong investor and creditor protection' (European Commission 2000, p. 8). Thus, our institutional analysis examines, first, the establishment of core accounting principles and associated systems of corporate governance and internal control (including audit committees) at the organizational level. Second, it considers the statutory audit and its external verification of management's compliance with financial reporting standards; with independent and objective auditors potentially sanctioning non-compliance by issuing an adverse audit opinion, qualifying it, or adding disclaimers. The public oversight system represents the third element of our FRES analysis. This is usually set up by the state, and typically features non-corporate bodies, independent of the accounting profession, who review audited financial statements and sanction any material lack of compliance—such bodies may be stock exchanges, securities regulators, government departments, privately organised expert review panels, or any combination of them (FEE 2001).

Previous research on the institutional FRES environment in Romania has featured descriptive studies on initial post-socialist accounting reforms (Delesalle and Delesalle 2000, Calu 2005), as well as empirical work on auditing (e.g. Albu et al. 2011, Cordoş & Fulop 2013, Păunescu 2015) and the country's move towards IFRS (e.g. King et al. 2001, Albu et al. 2014). We extend the empirical insights and analytical perspectives of prior research by considering such reforms in conjunction with the accompanying attempts to establish public oversight mechanisms for financial reporting and auditing. As such, we provide the first integrated study of the development of a post-socialist FRES. Acknowledging the complexities inherent in research that is informed by an institutional perspective (Thornton et al. 2012, p. 185), our study draws on two main research approaches to the collection of empirical evidence: a content analysis of publicly available regulatory documents, and semi-structured interviews with relevant actors in the accounting and auditing professional practice and regulatory arena in Romania. We first identified all publicly available regulatory documents, from the collapse of the country's socialist regime, in December 1989, until the end of 2016, that related to the emergence of the Romanian FRES. Relevant documents were retrieved from library, parliamentary, and governmental archives. They included capital market related laws, codes, and other regulations dealing with financial reporting enforcement in a wider sense, but also the annual reports and any other publications of relevant regulatory bodies, as well as parliamentary and governmental documents, such as protocols of hearings and legislative supplements relating to capital markets, corporate reporting, and auditing. Embracing an interpretative approach, these documents were subject to multiple rounds of content analysis. Two researchers, whose native language is Romanian, carried out the initial analyses independently,

discussed and consolidated their findings, and then deliberated over the outcomes with the third member of the research team. The aim of this analysis was to gather contextual information on financial reporting enforcement in Romania, develop an understanding of how the FRES formally emerged and evolved in the country, and to help to inform the subsequent interviews.

Semi-structured interviews were conducted with 20 people involved in accounting and auditing, including the regulation, supervision, and practice of financial reporting enforcement in Romania. Interviewees had various backgrounds, and included regulators, preparers, auditors, analysts, academics, members of professional bodies, and senior management of the WB.⁶ Several interviewees had experience in multiple capacities, and all of them had an in-depth understanding of the Romanian FRES. Interviewees were chosen to cover all relevant actors in the field, and to offer different perspectives on the subject matter in the specific context. Assuring full anonymity, we asked interviewees to elaborate on critical financial reporting enforcement events or developments that we had identified through our initial analysis of regulatory documents. The Romanian authors conducted the interviews between January and July 2016, in Romanian when this was the mother tongue of the interviewee (19 out of 20 interviews), and in English for the remaining interview. All interviews were held in person or via Skype. Interviews lasted between 30 and 95 min. 11 interviews were recorded and subsequently transcribed. When permission to record was not granted (9 cases), notes were taken and immediately transcribed after the interview had been concluded. Interviewees were provided with their interview transcript and invited to comment on and amend this document. Subsequently, the transcripts were revised as necessary. Following the transcription, all interviews were translated into English and shared among the research team.

The transcripts were first analysed in light of the chronology of key events that took place in the field of financial reporting enforcement in Romania, including accounting, auditing and capital market regulation. Main regulatory developments mentioned in the interviews were matched against the initial analysis of regulatory documents, with the interviewees' perception and interpretation of these events being identified. Based on prior studies of regulatory developments in accounting (e.g. Canning & O'Dwyer 2013), the interview transcripts were then analysed with a view to determine the relevant actors' engagement with the country's institutional environment, its resources, and the resulting enforcement practices within and between the three core elements of the FRES. The results of this dynamic analysis unfold in the narrative below.

Acknowledging that any type of translation adds another layer of interpretation to the materials (Xian 2008), several measures were taken to mitigate this issue. Regulatory documents were analysed in their original language, and only relevant excerpts have been translated into English, either for the purpose of informing the entire research team or to be used as illustrations in the study's narrative. While most of our interviewees were fluent or at least experienced in English, conducting the interviews in a person's mother tongue eased the conversation and allowed for a deeper explication and understanding of the interviewees' views. For the interviews conducted in Romanian, the interviewer translated the transcript. The other Romanian researcher, who was not involved in conducting the interview, then crosschecked the translation. Subsequently, the English translation was discussed by the entire research team (3 people) and modified, as deemed necessary, to facilitate comprehension in the English language. While these measures cannot rule out remaining translation issues, we are confident that the resulting analysis vividly demonstrates how a FRES of Western inspiration has been created and duly developed in Romania.

⁶Appendix 1 and appendix 2, both available online, contain, respectively, the full list of interviews with their details, and the guiding questions for the interviews.

4. Cultural traits and national politics in self-enforcement

Our analysis of the responses of Romanian accounting and auditing professionals to the establishment of the FRES after the fall of the socialist regime in 1989 indicates the relevance of the institutional resource environment for translating regulatory change into practice. Local managers and companies remained subject to institutional legacies. Being simultaneously exposed to pressures for continuity and change, local actors do not simply become institutional mimics who immediately assimilate new practices, but they require and/or depend on resourceful guidance to change established practices (Soulsby & Clark 2007). Even after the initial legislative accounting reforms were in place, the Romanian state did not embrace the role of an incubator and promoter in the creation of a national FRES as it continued to demand financial information primarily for taxation purposes. This continuity did little to stimulate corporate awareness of a need to change. The mixture of the country's ad hoc approach to regulatory changes, its notional political commitment to support the proper implementation of such changes, and certain key developments in the capital market environment ended up creating a varying level of pressure for corporations to change, leaving corporate management to navigate the resulting cultural and political tensions.

Immediately after the first accounting law (of French inspiration) had been passed in 1991, the Romanian Ministry of Public Finances organised training sessions to support the implementation of the new regime. Given the Ministry's financial and organisational resource constraints, the unavailability of trainers with sufficient expertise in both Western and Romanian accounting practices, and the accompanying need to translate from French⁷, these sessions were organised only in the country's four biggest cities (Bucharest, Cluj-Napoca, Timișoara, and Iași) and each one was limited to 400 participants. Furthermore, the short duration of these courses and the low technical skills of Romanian accountants in the early 1990s (Delesalle & Delesalle 2000, King et al. 2001) impaired the effectiveness of this governmental support mechanism. Such deficits in the resource environment meant that practices of self-enforcement changed only very slowly (Thornton et al. 2012). The socialist mentality of many managers towards the preparation of financial statements, largely reflecting a rules-based approach to accounting, and the habit of keeping financial and corporate information secret, remained largely unchanged for several years. Despite the change in legal and capital market requirements and the introduction of more comprehensive disclosure requirements, one interviewee recalled an experience in the early 1990s: 'There was a time when all the disclosures meant one page' (I9, Big 4 auditor). Companies continued to work under the principles of secrecy, accompanied by 'a communist attitude of total opacity and a lack of understanding of the role of financial statements' (I12, academic). Corroborating the persistence of socialist logics, this interviewee continued that 'during my first contact with the company [...], they told me that their financial statements are secret, and wondered why I asked to see them' (I12, academic).

Other interviewees submitted that the transition was aggravated by preparers' strict adherence to following protocols, filling in form sheets, and working along checklists:

It may still be the remnant of the communist time, a bureaucratic attitude, [...] that people here [in Romania] see 'yes' and 'no' answers, at all levels, which was the case in developed countries 30–40 years ago. There is not much emphasis on judgment. (I6, WB)

⁷This was particularly necessary for the training materials, which the French delegation provided. They comprised case studies, overhead projector transparencies, and the French accounting regulations (Delesalle & Delesalle 2000, p. 107).

The Romanian Ministry of Public Finances did not help this situation as it issued accounting regulations in a rush, without leaving companies sufficient time to prepare for the changes to their accounting systems:

In Romania the [regulatory] process is like this: usually the regulations are issued very late, for example in December, with immediate application, starting in January [of the following year]. [...] There are only a few people involved in designing the regulations, and they [the Ministry of Public Finances] have very short public consultation periods. You cannot convince a CEO to allocate resources if the regulator doesn't communicate, in the most serious and responsible way, the economic consequences and the impact [of the regulations] and their [the Ministry of Public Finances'] expectations. (I5, academic)

Another unfavourable institutional characteristic was national politics and the continuing privileging of taxation matters over financial reporting:

It was terrible. Everything was recorded for taxation purposes, nothing else mattered. I explained to everybody all the time: stop using the Tax Code for purposes of financial accounting. [...] But they [the preparers] targeted their financial statements to the tax authorities only, not to shareholders. (I19, BVB)

Based on a survey conducted in 1997/98, King et al. (2001, p. 163) suggested that the Romanian preparers' focus on tax accounting was actually incentivised by the government. Financial statements were mainly used by the state, foremost to compile national economic statistics and determine tax payments. Moreover, tax authorities would require the application of tax rules for the recognition of items in the financial statements. The situation did not change when the country decided to adopt international accounting standards. On the one hand, this was because many elements of the old accounting system were retained when IAS/IFRS were integrated into national accounting regulations, such that, for example, national rules continued to prescribe the use of a chart of accounts and specify a strict format of financial statements (Calu 2005). On the other hand, non-compliance with tax provisions was sanctioned much more severely than were violations of financial reporting requirements:

Not filing the tax reports on time is extremely onerous, while not filing the financial statements is only fined 4,000 RON [about 900 USD]. This is nothing. (I18, Big 4 auditor)

The result was that corporate managers paid little attention to the proper application of relevant accounting standards in the preparation of financial statements. They tended to perceive accountants as being primarily in charge of ensuring correct tax filings. This is why companies allocated accounting education and training resources predominantly to taxation:

Very few companies invest in their accounting staff to develop their finance and accounting skills, but they invest in tax training, as they perceive the tax authorities to be able to fine them. They feel threatened by them, so they see accountants as staff that keep them from being fined. (I18, Big 4 auditor)

Given these observations, it is not surprising that companies allocated only very limited resources to governance mechanisms, because:

In Romania management prevails. Audit committees do not exist or are very weak. This is another enforcement problem. Professionalising the audit committee is the first step of enforcement [...]. Moreover, there is a corporate governance problem. Many companies do not have a corporate governance culture. (I4, WB)

Table 1. Market capitalisation as % in GDP.

Country	1998	2005	2010	2014
Romania	0.8%	15.9%	8.5%	11.2%
Poland	11.8%	30.9%	39.8%	31%
France	65.2%	79.8%	72.2%	73.7%
UK	149.5%	126.4%	Not available	106.5%

Source: World Bank Indicators, 2016 - <http://data.worldbank.org/indicator/CM.MKT.LCAP.GD.ZS> [Accessed 20 May 2016].

Thus, regulatory demands in terms of corporate governance also had only a minor impact on actual practices. It is suggested that this is primarily due to the structure of the Romanian capital market and the associated corporate ownership environment, which were deemed unfavourable to the accommodation of Western modes of governance (McGee 2010).

After the Romanian stock exchange had been re-established in 1995, it continued for a number of years to comprise only a few listed companies.⁸ However, while being of little relevance in the 1990s, Romania's capital market flourished after the year 2000, when market capitalisation and transactional efficiency improved significantly, such that the millennium came to be considered as a turning point in the country's development (Filip & Raffournier 2010). However, Romania's stock exchange (BVB) failed to become a viable source of financing for Romanian companies, with bank loans providing most of the companies' capital, and continuing to do so today.

Thus, the country's capital market remains underdeveloped, even in comparison with other countries in the region (Table 1). Moreover, BVB is dependent on the Romanian state. Many companies are listed for public visibility rather than to attract equity investments, or they are controlled by, or have a significant holding of, the state. As a consequence, analyst activity is low. Traditionally, there has not been substantial public coverage of specific companies or industries in the country (I17, analyst), and hence there is little institutional pressure from financial statement users for companies to improve financial reporting.

As detailed by a number of interviewees, these circumstances have provided little incentive for serious corporate self-enforcement:

Some listed companies are controlled by one shareholder; they have very few market transactions. [...] The shareholder has all the information and does not want the company to be very transparent. (I3, non-Big 4 auditor)

Some of the listed companies got listed in order to escape from the influence of Fondul Proprietatea⁹, not because they wanted to be listed. To some extent, this was a good thing for the BVB, because otherwise the number of listed companies would have been even smaller. But these companies don't function like the regular listed companies. I mean, in a listed company there is an independent board of directors, and a manager is paid according to performance targets, and they all work in that direction. In Romanian listed companies that have the state as a shareholder, managers are appointed

⁸The number of listed companies in the Romanian regulated market constantly varies between about 60 and 80. Additionally, several hundred companies are listed in a variety of unregulated markets. The usual regulatory requirements for publicly listed companies, such as preparing audited financial statements under IAS/IFRS, do not apply in these unregulated markets.

⁹Fondul Proprietatea is a joint stock corporation operating as a closed-end investment firm without a finite life. The Fund was established by the Romanian government in 2005. Eligible claimants who lost property under former socialist governments were granted shares in the Fund in lieu of compensation.

for political reasons. They are old, have no management or financial expertise, and the companies just survive. When I was working in audit, we went to a big state-owned company. The people there shocked me, all of them, their way of working. It was just like they were stuck in time. I just wondered how this company could still exist. On the other hand, it is so difficult to change a company like this. Even if you change the manager, the people will be the same and it is so difficult to instil change. (I17, analyst)

Even large, listed companies seemed to neglect the allocation of sufficient resources to financial reporting, as indicated by our interviewees:

I remember a case from when I was giving an IFRS course for [one of the Romanian professional bodies]. There was a lady in the room literally in despair, because the board of directors of her company, a listed one, had not allocated any resources to IFRS implementation. It was November or December 2012¹⁰, and starting in January 2013 they were supposed to apply IFRS. (15, academic)

Only about 10% of our Romanian clients actually apply IFRS, the rest only check the box of having their trial balance transposed to IFRS, in a simple compliance exercise. When I tell a company that, in order to properly apply IFRS, they need to put in place a small support department to gather and provide the necessary information, they are shocked. (I18, Big 4 auditor)

It appears that this environment provided unfavourable endowments in institutional resources, and scarce incentives for companies to seriously commit to the preparation of their financial statements. Reluctance at the corporate level to undertake serious change can be seen to be a more general feature of institutional transition in the CEE region, where practices often only change after local institutions created incentives for ‘unlearning’ (Soulsby & Clark 2007). Our interviewees corroborated this observation when referring to regulators, users, and investors demanding changes in corporate self-enforcement practices:

It is a learning process. The low level of compliance might be triggered by the [institutional] difficulties related to the assimilation or application of IFRS, not necessarily by the intention to disobey. The fact that companies actually make the modifications to financial statements required by ASF [Autoritatea de Supraveghere Financiară - Financial Supervisory Authority, the current Romanian financial reporting enforcement body] is a sign of goodwill and evolution. (17, non-Big 4 auditor)

Some companies [now] have filters—internal audit, audit committee, corporate governance, a serious auditor—whereas others just pretend they have these, and the difference is visible in the quality of their reports. (15, academic)

The ‘old’ approach was that accountants were there ... somewhere [interviewee smiles and pauses]. The management of listed companies begins to understand that they need to hire qualified accountants, and how they should use them to prepare the reports and manage internal controls. (I19, BVB)

What appears to be a most relevant mitigating factor that encourages companies to take self-enforcement more seriously is foreign ownership, or the demand for foreign capital more generally:

Most listed companies were confused and puzzled about the first-time application of IAS, particularly the ones that operated for a long time, shipyards for example, and had a ‘communist’ activity. They were clearly old-fashioned, and they did not have the information available nor the systems that could

¹⁰While listed firms have had to use IAS/IFRS to prepare consolidated financial statements since 2007, in 2012, the Romanian Ministry of Public Finances extended the application of IAS/IFRS for listed companies to their separate financial statements (OMFP 1286/2012 Art.5).

provide them with the data required to apply IAS; therefore, this was a 'heave-ho' kind of implementation for many of them. They needed to have an incentive to apply IAS properly. I noticed, for example, a big improvement whenever a company had foreign funding. Otherwise, it is just another OMFP [Order of the Minister of Public Finances] that got published, and they needed to put in yet another amount of money without value added, just to comply with it as well. It is very difficult for accountants to 'sell' this to a manager or the board of directors. (I18, Big 4 auditor)

In essence, crucial to the effectiveness of a FRES is a demand for compliant financial information, and for corporate management to be aware of the importance of financial reporting. Any deficiencies identified in self-enforcement immediately direct attention to the effectiveness of the second element of the FRES and the following section of the paper duly discusses the role of auditing and auditors in the development of the FRES in Romania.

5. The Western push towards the emergence of auditing

Auditing is a control mechanism for corporate management's financial reporting. Within an effective FRES, auditing is said to contribute to a country's investment and capital market environment by providing assurance that corporate financial information is reliable, and by drawing public attention to cases of non-compliance (Brown & Tarca 2005). In the wake of the post-socialist transition, a Western conception of auditing, which was fundamentally different from local habits, understandings, and practices, arrived in the CEE region. Under Romania's socialist regime, auditing, in the sense of an independent institution that publicly verifies that a company's financial statements comply with the applicable accounting standards, had not existed. Corporate monitoring was dominated by state control over companies, exercised through regular on-site inspections and continuous monitoring by the Ministry of Public Finances. It aimed to assure the proper use of state funds, and to achieve the state's production and productivity targets (Calu 2005). Hence, when the socialist regime fell, there was no established professional oversight that could mitigate the limitations evident in self-enforcement. With the support of Western actors, an audit infrastructure had to be created in parallel to the new accounting and corporate regulation (King et al. 2001).

Between 1991 and 1994, the same team of French experts who had assisted in drafting Romania's 1990 Companies Act and the 1991 Accounting Act, also supported the creation of Corpul Experților Contabili și Contabililor Autorizați din România (CECCAR – Body of Expert and Licensed Accountants of Romania). CECCAR members covered all areas of accounting and they were mandated to conduct what was seen at the time as statutory audit¹¹ (Delesalle & Delesalle 2000). Based on positive experiences in other countries of the former Soviet Bloc and diagnosing that 'audits' performed by CECCAR members were often of poor quality, the WB and the IMF demanded the creation of a separate national professional body for financial auditors (King et al. 2001).

Thus, in 1999, such a body was formed. Camera Auditorilor Financieri din România (CAFR – Chamber of Financial Auditors of Romania) assembled the country's financial auditors who were, from then onwards, the only group of accountants qualified to act as statutory auditors. The establishment of CAFR was part of the general drive to further westernise accounting in Romania in the late 1990s. As CAFR was in charge of proposing Romanian auditing standards based on ISAs, the creation of this body also facilitated Romania's enactment of the EU's 8th Directive on Statutory Audit. To safeguard the functioning of the statutory audit as the second element of a

¹¹Financial statements of firms with limited liability had to be checked by three 'censors', who had to be employed by the company, and one of whom had to be a CECCAR member. CECCAR considered this form of internal control as audit (CECCAR 2006).

country's FRES, it has been held that audit quality has to be comparable across different auditors and auditing regimes (FEE 2001). Although CAFR had been created in 1999, it only implemented a quality control process between 2006 and 2008. CAFR quality inspections of audit firms were said to be rather symbolic (I2, CSIPPC). They normally lasted not more than 10–20 h, and primarily focused on the existence, not the substance, of audit documents. This lax approach to audit quality within the profession's oversight was symptomatic of the weak standing of auditing in the local context.

Moreover, public and corporate resources for enhancing the accounting and audit functions remained scarce. Realising this, the IMF and WB intended to 'encourage the development of an accounting and auditor training industry' (King et al. 2001, p. 167) by forming CAFR. The WB specifically provided funds for an initial audit training programme for 500 preparers, users, and financial auditors. However, the desired training industry did not develop, and auditing continued to remain an alien concept:

Some managers do not understand the concept of audit. They believe that they are responsible for the statutory, usually tax-oriented reports, while auditors are responsible for the IFRS financial statements (I1, non-Big 4 auditor).

With the government not allocating the required resources to audit educational initiatives, the only visible educational offerings were the continuous professional education courses that CAFR offered to its members and the audit firms' in-house training activities. With regard to the latter, the Big 4 audit firms had an advantage, because they were able to draw on their international resources. When they opened offices in Romania in the early 1990s¹², their networks sent international colleagues into the country, provided access to Western accounting and audit procedures, supplied resources for comprehensive in-house training sessions, and supported the idea of creating CAFR. While Romanian auditors employed by the big international firms benefited from these firms' resources, those working for national firms did not. Based on a comprehensive literature review and numerous interviews with Romanian audit professionals, Albu et al. (2011) concluded that there was a significant gap between the perceived audit quality of local and Western firms. Several of our interviewees attested to this disparity, for example:

When we talk about small practices, we cannot but question how much experience they have in auditing IFRS financial statements, especially [those] issued by large companies. (I19, BVB)

Local [audit] firms are employed only by managers not interested in the quality of audit. (I2, CSIPPC)

I know from colleagues inspected by the ASF that they [ASF] recommended to change the auditor to a Big 4 one [...] I see a big difference between Big 4 and non-Big 4 [audit quality]. (I17, analyst)

Given their advanced training according to international standards and practices, especially in terms of IFRS accounting, the big audit firms played a significant role in educating the preparers of corporate accounting reports (Albu et al. 2014). For example, Albu et al. (2011) found evidence of Big 4 auditors imposing strict IFRS implementation schedules on their clients, including pre-tests of the new standards, and working closely with them in preparing the first sets of IFRS-based financial statements. Our interviewees reinforced the existence of educational challenges in Romania's creation of a post-socialist audit function within its FRES, and the educational role of Big 4 auditors in relation to IFRS adoption:

¹²For example, according to their websites, PwC have had a Romanian office since 1991, EY and Deloitte since 1992, and KPMG since 1994.

The first year of IFRS application is extremely difficult, especially when you work with a Big 4. Blood spills. But the process improves over time [...]. We need to have a learning process in place, people need to be helped to understand why this [transitioning to IFRS] would be useful, not fined because they did not file or complete correctly [emphasised through gestures] whatever form. The auditor should also play a very important role in the enforcement process, through supporting the companies, not by focusing on compliance. (I18, Big 4 auditor)

Nonetheless, the practical impact and power of auditors to serve as an effective control element of Romania's FRES continued to have evident limits. Many auditors had insufficient resources to conduct audits in the Western sense, and this situation was tolerated under a superficial quality control regime for many years – just about half of all listed companies being audited by Big 4 firms or firms that are members of international networks (Păunescu 2015). Furthermore, the visible outcome of the audit process, namely the audit opinion, was not particularly relevant in the local context. For example, in an analysis of the first tier of the Romanian capital market, which comprises the largest, and thus most important and visible companies, Cordoş and Fulop (2013) reported that between a fifth and just over a third of annually issued audit opinions were qualified between 2008 and 2012. ESMA (2017) considered these findings to be 'indicative of poor internal controls within issuers and [...] the ability and/or willingness of issuers to apply the relevant financial reporting framework' (p.21). This diagnosis also raises questions as to the role and effectiveness of public oversight including substantive reviews of audited financial statements in the Romanian context. This is the focus of the following section of the paper.

6. The dependency on national governmental and Western resources for setting up effective public oversight

Until 1989, corporate public oversight was limited to the central government and its direct monitoring and controlling of all enterprises. This system aimed to ensure the functioning of the planned economy and did not involve any private intermediaries (King et al. 2001). CNVM, the Romanian stock market regulator, was established as the country's first public oversight body for financial reporting after the fall of the socialist regime. It was set up in 1994, as 'an autonomous administrative authority' (Romanian parliamentary law no. 52/1994 Art. 5), funded by the Romanian state (Art. 7), with its members appointed by parliament (Art. 8). Being responsible for supervising the financial markets and safeguarding investors' rights 'to have access to reliable, correct and sufficient information that is made public in a timely fashion' (Art. 79), CNVM was mandated to 'issue appropriate regulations to ensure investors' access to information, and [...] enforce their application' (Art. 79).

However, the state did not endow CNVM with the resources necessary to fulfil these tasks effectively. Thus, in 1999, CNVM was granted approval to secure funding through levies imposed on the companies to be regulated (OUG - Government Emergency Ordinance 6/1999). Despite this change in their funding structure, the regulator's resource endowment remained tight. Realising this deficiency, CNVM approached the Romanian parliament arguing that the government had not provided sufficient funds to set up the infrastructure necessary to fulfil the tasks legally assigned to CNVM. Illustrative of how devastating the situation was, CNVM claimed that they were not provided with enough suitable office space, and that they were denied investments in duly needed information technology (CNVM 2001). In response, the government marginally amended CNVM's levy and funding structure (OUG 25/2002). Nonetheless, this did not improve the regulator's constrained resource situation (CNVM 2006). CNVM's employees continued to work on a low pay scale compared to the private sector. Its staff turnover was high, with well-qualified and specialised personnel frequently leaving for

non-governmental employment. This led the WB (2004) to conclude that CNVM's resources were insufficient to accomplish its mission and to push for a further reform.

Facilitated by the WB and the EU, Romania's 2004 reform of the FRES formally empowered CNVM 'to ensure that the public is correctly informed' (Romanian Parliamentary Law No. 297/2004, Art. 234c) and to introduce a fining scheme for companies not complying with the requirements to prepare and publish audited financial statements (Art. 273). The regulator was given the legal capacity to demand additional financial information directly from auditors, if necessary (Art. 260), and to approach the professional audit body, CAFR, to report potential shortcomings in a company's audit process (Art. 263). The EU and the WB also sought to provide further training to CNVM's staff, suggesting procedural enhancements, and to assist the regulator in upgrading its technological infrastructure by jointly developing and implementing an electronic filing platform for corporate financial information (CNVM 2006).¹³

Despite such developments, however, the resourcing situation of CNVM remained insufficient, and it continued to be predominantly occupied with chasing companies to file financial statements:

Regarding the compliance with the reporting obligations, in March we notified 1,716 issuers about the submission deadline [...] in June we brought to the attention of those 779 issuers who did not submit their [corporate financial] reports, that they had disobeyed the legal requirement. (CNVM 2009, p. 45)

The public oversight body's deficient resource endowment explains why, despite the evident weaknesses in the audit element of the Romanian FRES, our interviewees observed that 'CNVM was not very much involved in enforcement' and 'relied very much on auditors' (I19, BVB), although the nature of such reliance was also questioned:

The regulator rushes and issues a regulation, companies don't understand its meaning and consequences, they do not allocate resources, the accountant is overwhelmed, the auditor comes in and *does not want to lose his client*, and they [the CNVM] say: these financial statements state 'IFRS', they are audited, so for me everything is fine. (I5, academic, emphasis added)

Corroborating this precarious condition of public oversight in the country, the WB (2008) concluded that 'no evidence of enforcement relating to financial statements has been found in the last two years in [...] CNVM's [...] annual reports'. This was because these reports contained merely declarative statements outlining CNVM's fundamental aim to achieve capital market transparency, and describing its legal role in supervising issuers. At this time, the national public oversight body did not appear to engage in material practices of enforcement, because of its limited resource budget and the on-going need just to get companies to file their financial statements.¹⁴

This position, however, started to change when the EU entered the scene. Acknowledging that 'there are diverse, historically contingent, and complex national solutions, deeply embedded in the institutions, values and established practices of specific societies' (Scharpf 1999, p. 192), the EU has always been well aware of the divergence between logics and practices in its member states. Historically, the EU did not seem to be particularly concerned about Romania, probably because the

¹³Indicating the amount of administrative work involved in the regulator's enforcement activities, CNVM (2006, p. 62) reports that they receive about 20,000 corporate paper filings per year.

¹⁴Apart from interviewees who stated that '[t]he Romanian supervisor is obviously more constrained [in resources] than its Western counterparts, even by reference to Poland' (I6, WB), the constant negotiations between CNVM and the Romanian government over resource endowments and funding, as discussed above in this section, speak to this problem.

country ‘has a very small capital market’ (I8, ESMA). The insignificance of the capital market implied that there was not much demand for internationally comparable financial information. It was only after Romania joined the EU, in 2007, that the CNVM began to engage seriously with the adopted frameworks, for example by starting to check audited financial statements for compliance with applicable accounting standards (CNVM 2009, p. 46):

In May 2008 the activity of checking the compliance of financial reporting with national accounting regulations and IFRS started. The verification is performed in accordance with the principles stated in CESR Standard no. 1. The reports of the issuers from the regulated market were checked following a procedure of selection based on the risk profiles of the issuers.

Triggered by the 2008 economic crisis in Europe and adhering to the subsequent developments aiming to create unified financial market oversight bodies in the EU, in 2012 the Romanian state installed a general financial services and market regulator (OUG 93/2012). CNVM was, thus, superseded by the newly created ASF (Autoritatea de Supraveghere Financiară - Financial Supervisory Authority), which took over and reorganised the responsibilities of the CNVM, the Comisia de Supraveghere a Asigurărilor (Insurance Supervisory Commission), and the Comisia de Supraveghere a Sistemului de Pensii Private (Private Pension System Supervisory Commission). By unifying these three supervisory bodies, it was hoped to enhance public trust in the Romanian financial market and to facilitate further integration within the EU.

In the ASF, the Issuers Transparency and Reporting Department (organised under the Issuers, Transactions and Market Abuse Monitoring Directorate) became responsible for the supervision of issuers listed on the regulated market. It analyses financial reports, demands their amendment if they do not comply with legal requirements (ASF 2014a, Art. 138), and generally exercises authoritative, regulative, supervisory, and control powers. Although not specified in detail, these powers do enable the ASF to take any measures that contribute to the market’s ‘stability, competitiveness and well-functioning’, including the option to impose sovereign sanctions (ASF 2014a, Art. 5). Overall, interviewees shared the view that the creation of the ASF had served to strengthen the public oversight element of the Romanian FRES:

The market and the ASF were restructured, and positive effects are visible. They are more professional, and they do a better job. (I17, analyst)

Historically, CNVM was a weak institution, while ASF is stronger, it attracts better people and has a deeper voice. (I6, WB)

Human resources are the key theme here. It has been said that knowledge relating to the creation, maintenance, and dissemination of how to turn Western principles into meaningful practices, and knowledge of the local environment and its determinants are essential characteristics for everyone working in the reformed space of post-socialist countries (King et al. 2001). Our interviews corroborate this view when specifically talking about the employees of public oversight bodies in Romania:

Similar to other people in the World Bank, I believe that there is not enough capacity for compliance, including resources and knowledge. (I4, WB)

To effectively conduct verifications, you have to hire people with a high level of experience. This is a big problem for us [the Council for the Public Oversight of the Accountancy Profession], and I think this is a problem for ASF as well. (I2, CSIPPC)

For an effective and efficient enforcement system, they [ASF] need to understand the features of every listed player as only then will they [ASF] be able to ensure comparability. They also need experts who are able to provide guidance on very sensitive issues. (I16, preparer)

However, people with such skills are also in high demand by the private sector, that can pay much more competitive salaries. ASF (2016, 2017) has acknowledged this issue, emphasising that securing and strengthening the human resource and IT infrastructure remain organisational priorities. They continue to work on capacity-building projects with organisations such as the WB, ESMA, and peer enforcement bodies, suggesting that further improvements are likely to continue to depend on Western assistance.

One of the Big 4 audit firms has also made a direct contribution to developing the ASF's practices, working with the enforcement body to develop a checklist for the screening of audited financial statements (I3, non-Big4 auditor):

ASF now has a detailed checklist and they check in detail the annual reports. They also ask questions about the audit opinion, and, if auditors make recommendations to managers, whether these were implemented.

Such a checklist provides the regulator with 'a frame of objectification' (Mennicken 2008, p. 399), which could be said to be of use in helping to establish a more predictable enforcement environment. However, this approach seems to put little emphasis on the specifics of particular companies, industries, or transactional circumstances. Thus it might just trigger more boiler-plate disclosures—exactly the type of corporate reporting that ESMA (2015) has said it wishes to avoid—but it also gives rise to calls for implementing more professional values and judgment in ASF's enforcement practices, as well as a more principles-based accounting culture:

They [ASF] have a checklist and map it to financial reporting. I think that there is other information that is more relevant than this but it is not reviewed. I think they are good but not great, because they see us strictly in a standard way. I think that they are young people who read a lot, they might have worked as well, but not too extensively, [...] and then, so as not to make mistakes, they have the checklist. [...] I saw multiple companies getting the results from the [...] checklist. It looked like as if it was copy-pasted to everybody. (I3, non-Big 4 auditor)

ASF has demonstrated awareness of these shortcomings, and appears to be convinced that the checklist approach is an appropriate tool 'to achieve a basic level [of compliance], necessary for the next step, which will be to improve professional judgment' (I14, ASF). Other interviewees agreed that this approach might be a suitable first step to improve financial reporting, given Romania's accounting legacy of 'starting with a balance sheet and income statement and, after that, learning how to write notes. But still the checklist approach tends to incentivise people to write long but useless reports' (I12, academic).

Internationally, ASF's efforts are recognised, but the body is continuously reminded to strengthen further its enforcement approach, with a particular emphasis on human resources:

ASF must give its staff the time and the space to do a thorough job, to carry out meaningful examinations, covering all areas of financial statements, and to take effective actions. (ESMA 2017, p. 22)

Acknowledging ASF's efforts to facilitate a cultural change in the Romanian FRES, by employing an approach that takes the country's institutional particularities into consideration, some interviewees called for more authoritative actions, and want ASF to:

sanction the lack of compliance. I think that the time of 'nicely asking' has passed [...] proper enforcement would also trigger companies to hire staff that are better qualified and that would result in an increase in accounting knowledge. (I1, non-Big 4 auditor)

The fines would increase the level of compliance. Accountants and preparers are afraid of receiving fines. If the company is fined, the management blames the accountants. And this is how the accountants will pay more attention to accounting. (I13, Big 4 auditor)

Yet, in Romania, authoritative enforcement sanctions are primarily used in conjunction with encouraging the (timely) filing of annual reports. They are rare in relation to violations of applicable accounting standards, even though non-compliance is common¹⁵ (CNVM 2011, ASF 2014b). This is because ASF prefers to employ a gradual approach to enforcement, allowing companies to learn throughout the process. In response to non-compliant financial statements, ASF orders companies to restate their financial statements, and companies usually comply. ASF often supplements such orders with recommendations on how to change reporting practices and processes, and it monitors how these are implemented. In case this in itself is not successful, they would even propose a change of auditor to the company. For example, IFRS became mandatory for the 2012 individual financial statements of listed companies, including the declaration that ‘financial statements shall not be described as complying with IFRS unless they comply with all the requirements’ (IFRS Foundation 2012, IAS 1.16); yet ASF revealed that 28 out of the then 79 listed companies failed to comply because their ‘IFRS financial statements’ were prepared based on Romanian standards and legislation (ASF 2014b). In consequence, the companies were ordered to restate the respective financial statements.

In essence, ASF’s ‘soft and staggered’ approach is rooted in its belief that fines or the name-and-shame approach used in other EU member states are not an effective means of increasing IFRS compliance in Romania (I14, ASF), a perception that can be connected to the country’s cultural, historical, and institutional specifics (Thornton et al. 2012). One interviewee referred specifically to the use of sanctions under the country’s socialist regime, and how this led to people just ticking boxes:

I do not believe that coercion is positive, as it merely leads to compliance and does not improve the financial education of businesses and managers. (I18, Big 4 auditor)

Even Western actors acknowledge that a cultural change in accounting, a move from technocratic record keeping to financial reporting based on professional judgment, can hardly be achieved by sanctions:

You have to have a strong regulator, but I am not sure about sanctioning. You’d be better having proportionate measures. No ‘black or white’ decisions should be made, rather the judgmental skills should progress over time. (I6, WB)

Furthermore, the small number of listed companies and the state’s interest in strengthening the local capital market precluded ASF from taking more serious actions:

I think that one of ASF’s objectives is to attract more companies to be listed [...]. Their lack of firmness might be interpreted as a desire not to lose some of the listed companies. (I12, academic)

They [ASF] will not delist anybody, it would be bad for the image of the capital market. (I3, non-Big 4 auditor)

¹⁵For example, in 2010, 50 out of the 69 listed companies were required to restate their financial statements, under national regulations (individual financial statements) and IFRS (consolidated financial statements) (CNVM 2011).

The enforcer's experience with some large listed entities around the year 2000 is illustrative of this situation. In fact, there have been cases where public entities tried to use their listing as leverage to avoid IFRS reporting. Albu et al. (2014) discussed listed Romanian investment funds, organised as groups, which for years had not complied with the requirement to prepare IFRS consolidated financial statements. Their managements had argued that this was because their subsidiaries did not provide IFRS data in the separate financial statements, so the cost for preparing consolidated IFRS financial statements would be prohibitively high. Acknowledging this deficiency, the national enforcement body attempted to change the underlying accounting regulations, and 'in 2008 CNVM required the Ministry of Public Finances to extend the scope of IFRS to subsidiaries of the groups required to consolidate under IFRS' (Albu et al. 2014, p. 505). In fact, given these cases and responding to a similar recommendation the WB had made, the Ministry of Public Finances eventually mandated the use of IFRS in the separate financial statements of listed companies in 2012. This change in the scope of IFRS application equipped the public oversight body with a reference to counter shady corporate arguments for non-compliance (I3, non-Big 4 auditor).

We conclude that the creation and functioning of the public oversight system in Romania is the result of the dynamics between Western and local pushes and pulls. Right after the collapse of the socialist regime, the state was busy with implementing the most pressing institutional prerequisites to turn the country from a planned into a market economy. CNVM, the first public enforcement oversight body created after the fall of the socialist regime, was institutionally weak and ill-equipped with resources. Although it was modelled along Western enforcement ideals and practices, this body's resourcing situation remained insufficient, such that it could only partially fulfil its tasks. Public oversight practices were non-existent for many years, which reflected deficiencies in self-enforcement and an on-going process of developing the FRES' auditing element.

This all changed when the country joined the EU, as compliance with EU regulation also meant paying much more attention to IFRS and related enforcement measures. A much bigger, more powerful, and increasingly aware financial supervisory authority (ASF) was created and enforcement practices began to change materially. Regulatory action started to shift from the monitoring of the timely filing of corporate reports towards assessing and verifying the scale of compliance of audited financial statements with applicable accounting standards. This transformation of practices was significantly and actively supported by the Big 4 firms. In conjunction with the EU requiring enhanced public oversight, it triggered an increase in governmental resource allocations, and eventually a change in the enforcement practices. Even though it does not always fully comply with the requirements mandated by the EU, and although there is still a shortage in its resource endowment, the ASF did develop and now deploys an enforcement approach that addresses and seeks to change the institutional and cultural specifics of the national context. It focuses on corporate learning instead of drastic sanctions.

7. Concluding discussion

This paper has analysed Romania's implementation of a FRES after the collapse of its socialist regime in 1989. This case serves to illuminate the transformation processes of emerging economies seeking to embrace Western standards and norms. Our findings are of relevance to key local actors in aspiring and emerging economies, as well as to Western bodies, and private and professional organisations involved in the promotion and dissemination of standards and norms.

Romania launched a FRES of Western inspiration to accompany the post-socialist marketisation of the country's financial economic and reporting environment. Western accounting standards and governance frameworks were translated into national laws and codes through a number of consecutive reforms. Various Western actors (in particular the French government in the early

days, later also the British government, the WB, the IMF, and the EU) provided initial resources in the form of training and education initiatives, advice, and technical support. Being involved in the transition of Romania and many other countries of the CEE regions, these actors had in mind, ‘a model of market perfection to which the United States is assumed to approximate more closely than most other so-called market economies’ (Child & Czeglédy 1996, p. 172), and they expected ‘the radical redesign of economic institutions to produce an end-point that resembled a pure form of market capitalism’ (Soulsby & Clark 2007, p. 1427). However, even for them it was an ‘unchartered territory’ since ‘no one [...] knew for sure how to create a market economy from scratch after decades of distortions under central planning’ (Roaf et al. 2014, p. 7).

Post-socialist national politics in Romania were mainly concerned with pleasing the international constituency. The state amended the body of law to demonstrate that the Western demand for reforms had been met, but did little beyond this. It had neither implemented incentives nor allocated sufficient resources to provide the continuous support required for the translation of the new standards and frameworks into sustainable practices of national actors, such as accountants, auditors, and corporate management. In this context, a major factor of concern was the underdeveloped Romanian capital market. Even after the recreation of the national stock exchange, the market continued to be dominated by listings of companies controlled by the Romanian state. This meant the local setting lacked demand from private investors or analysts for high quality financial information.

As a result, accounting practices did not follow the new, legally inscribed logics (Tilcsik 2010, Kern et al. 2018), and corporate self-enforcement, as the first element of a FRES, remained weak. The initial top-down reform of financial reporting enforcement inspired only minimal changes at the preparers’ level. Accountants continued to work in a fashion reflective of the old cultural traits and remained committed to secrecy and an internally oriented, technocratic, rules-based approach to accounting, ultimately impairing the effectiveness of the Western institutions that had been established as part of the new FRES.

We argue that the local audit culture reinforced this lack of development. Auditing in the Western sense, as the second element of a FRES, did not exist when Romania transitioned into post-socialism. Relevant institutions and knowledge had to be created locally, and could only be provided by Western actors. Apart from the WB and the IMF, the Big 4 audit firms and local firms who joined international networks actively engaged in the development of the FRES. As supporters of IAS/IFRS and ISA, the Big 4 firms played an important educational role and committed financial and human resources toward the creation of the Romanian FRES as soon as they entered the country in the 1990s. Granted, in some instances, their involvement went beyond what one would conventionally anticipate and tolerate in developed economies. For example, in the early 2000s, Big 4 firms were at times involved in the preparation of IFRS financial statements which they audited afterwards, while in the 2010s one of the Big 4 firms was instrumental in the local enforcement body’s development of a checklist for the inspection of audited corporate financial statements. As such, these firms have continued to have a significant impact on institutional features and relevant practices in the development of the Romanian FRES.

Noticeable improvements in the third FRES element, namely public oversight, became visible around the country’s EU accession. This finding re-emphasises the power of Western organisations as a potential ‘main driver of structural change’ in emerging economies (Roaf et al. 2014, p. vii). In fact, the EU still provides an on-going stream of resources to the Romanian public oversight body, be it in the form of regular governance reviews, technical infrastructure development projects, or the knowledge exchanges within ESMA’s coordinating enforcement efforts on the trans-European level. Employing what may be regarded as its own customised approach to enforcement practice, based on less judgment and weaker sanctions than are common in developed economies, the local enforcement body recently has appeared more

committed to stimulating change in actual practices. It could be argued that these ensuing local modifications of Western institutions of financial reporting enforcement have helped to facilitate the local acceptance of the new institutions, because they take into consideration the national specificities resulting from a unique combination of history, culture, and politics. Nonetheless, it remains to be seen if these local adaptations may, similarly, deliver limited changes in the overall quality of financial reporting.

Considering that ‘formal structures travel more quickly than knowledge and expertise’ (Menickken 2008, p. 402), even the most prominent Western actors admit that they underestimated time as a critical factor in Romania’s development of a FRES:

An improvement exists, but it takes time ... if some time ago we thought that in four or five years [...] everything will be done, we now estimate that it will take rather ten or 15 years. [...] You can’t impose enforcement and supervision if no one asks for them or understands what they are. (I4, WB)

We conclude that material changes in enforcement should be expected to become visible only after a longer period of time, especially in terms of functional or operational impact. Arguably they manifest only when there is an alignment between national and Western actors’ expectations. Change emanates through mutual learning processes that need to be engrained in local actors, such as financial statement preparers, auditors, and users. The un-learning of the past and the adoption of Western practices at the micro-level depends on suitable incentives for change. Western actors may provide such incentives, but will first need to understand which incentives work for which national actors. For example, the appropriate balance between the respective deployment of sanctions and educational initiatives as authoritative means for financial reporting enforcement has to give serious attention to local circumstances and context. In asserting the vital importance of compliant financial reporting, the FRES has to allow time and space for the acquisition and application of the resources necessary to change past practices. Market-based practices promoted by Western bodies, international accounting firms, foreign investors, and subsidiaries may only be capable of permeating slowly into emerging sites, and only if accompanied by sufficient, targeted, financial and, in particular, human resources.

Finally, our findings emphasise the limiting role of the national state in transforming indigenous and setting up new institutions, often intended to augment the role of financial markets (Arnold 2012). Emerging states may deploy their sovereign powers to adopt Western standards and frameworks in national codes, laws, and other regulations. However, as they also decide the scale of resources to devote to the actual implementation of these norms in practice, they can also have a significant impact on whether the institutions they create are effective and function as intended or remain symbolic shells. In particular, the Romanian case demonstrates how a lack of state commitment to newly created and transformed institutions contributed to delays in the building of an effective FRES in an emerging economy. Although useful and necessary institutions and organizations were swiftly created after the fall of the socialist regime, little was done to promote them. They were not provided with the resources necessary to engage in activities that could have changed old practices more rapidly. Arguably, the Romanian state suspended its commitment to setting up a FRES as soon as it realised its international constituents were satisfied, and reallocated resources to other projects.

As national regulatory settings and arrangements increasingly are expected to yield to Western regimes (Botzem 2014), national states find their traditionally uncontested hegemony over regulation challenged and any pursuit of regulatory change will be charged with the task of overcoming or countering the resulting tensions. Basic issues of resource availability will inevitably be a key consideration, but the scale and impact of regulatory reform initiatives is fundamentally going to depend on how shifting political considerations and persuasions impact on the commitment to deliver and facilitate material change in local sites. In this regard, the stark contrast between the

socialist and the newly advocated market logics is likely to mean that such a political dynamic will remain significant in former socialist nations, making them continue to be rich and fruitful empirical settings for institutionally-informed research (Thornton & Ocasio 2008, Thornton et al. 2012). In particular, there is much potential in considering the role that educational initiatives can play in influencing the functionality of a national FRES and facilitating change in the wider legal and political systems.

In concluding the paper, there is one additional issue to highlight as a point of reflection and potential for further research.¹⁶ This derives directly from the persistent suggestion of Romania being a country where corruption levels are said to be relatively high (Transparency International 2020). Corruption can be practiced through interventions in the legislative process, blackmail and threats, unwritten agreements and conspiracies, or the provision of funds and various resources to politicians, parties and other influential bodies (Graycar & Monaghan 2015), with a considerable capacity to impact on individual and corporate behaviour (Zakaria 2018). Further, while corruption can be an endemic feature even in contexts characterised by well-functioning systems of government, it is typically said to be more vigorous in emerging and transitional economies (Neu et al. 2013). Such observations and claims could be used to suggest that the operationalisation of the FRES in Romania has been more superficial than substantive, driven more by impression management desires than the pursuit of fundamental, systemic change. In all of our concentrated study of the construction and developing application of the FRES in Romania, we did not come across any explicit cases or consequences of corruption in relation to financial reporting processes, although it could be argued that these are not things to which research participants would readily admit and, by their very nature, are likely to be practised and pursued in ways which ensure their exclusion from regulated financial reporting processes that are publicly documented. As such, we are in a position where we can neither claim that the FRES has had a dramatically positive impact on the prevalence of corruption, nor rule out the possibility that corruption has to some extent influenced the practical development and operational efficiency of the FRES in Romania. Going forward, this is an empirical test that any FRES will have to confront. In this regard, we would lend support to Jeppesen's (2019) recent argument that corruption has to be a research issue that accounting scholars need to devote more attention to, especially those with an interest in the operation of financial regulatory systems and their enforcement capacities, and particularly in countries that have exhibited higher degrees of institutional instability and political influence, such as post-socialist and transitional economies.

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¹⁶We thank the special issue guest editors for suggesting this point.

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