

# Nations' Cultures Impacts on the Accountants' and Auditors' Behavior and Actions: Comparing Islamic Tax and Traditional Tax System from the Aspect of Social Responsibility

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## ABSTRACT

Since the 1960s public corporations in the United States have faced increasing expectations from various stakeholders to become more socially responsible. This pressure has significantly increased over the past two decades fueled by public outcries for socially responsible corporate behavior following the fraud scandals of the early 2000s such as Enron, Tyco, WorldCom, and HealthSouth. These frauds also led to increased government regulation and oversight of public corporations, boards, and the audit profession. Internationally, the call for corporate social responsibility has also increased. The dimensions of a nation's culture effect the expectations its society exerts over corporations related to corporate social responsibility. Additionally, these dimensions effect the manner and level in which corporations actually engage in corporate social responsibility. Carrol (1979, 500) states, "Corporate Social Responsibility encompasses the economic, legal, ethical, and discretionary (philanthropic) expectations that society has of organizations at a given point in time." In order for philanthropic expectations to be satisfied by corporations in the United States, voluntary philanthropic actions may be taken. Such actions may be rewarded through reduced tax liability. While some corporations take significant action to satisfy this expectation, many firms do not engage in philanthropy since it is discretionary. These corporations typically take action if there is a perceived benefit that exceeds the cost. In certain countries such as Saudi Arabia, corporations are required to satisfy philanthropic expectations through a "religious tax," which is called Zakat. This method is used in Islamic laws in several Islamic countries and is based on the holy book of the Quran and the message of Prophet Mohammed. In fact, Zakat has some strict regulations for who pays and who receives the payment. However, the United States is a country that values freedom where no specific religion is supported by the government. This freedom supports to the concept of having philanthropy be discretionary in nature. Our current study investigates how the dimensions of a nation's culture impacts the manner and degree to which corporations engage in social responsibly and the related taxing outcomes. We discuss elements of Zakat and taxation as one means of pursuing corporate social responsibility based on national culture.

**Keywords:** Cultures' Nations, Social Responsibility, Fraud, Governmental regulations, Audit, Ethics, Islamic Tax, Accounting, Traditional Tax system, Fair, Significance, Influence, Positive

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## INTRODUCTION

### Social Responsibility Definition

Social responsibility is the situation where every individual is expected to take up their civic duty. In which case, an individual's actions have to be of benefit to the whole society. Corporate social responsibility on the other hand is the practices and policies followed by corporations that are meant to create a positive impact in the society (Ethics Unwrapped, 2017). Social responsibility is a tool to maintain the operations and to get involved with the society and hence the CSR is endorsed in the business core and considered as a matter of strategy.

Corporate Social Responsibility is looked as a business perspective to address sustainability to take the responsibility of the impact caused to the environment, society, and the economy due to the company operations (Carroll, 1979). This social responsibility adds value to the business process by making an effort to increase the level of business transparency and the core pillars on which the social responsibility of businesses or individuals resides are the minimum harm, maximize

benefits, be accountable and being responsive to the stakeholders. In various researches, it is analyzed that higher ethical values of managers reflect higher CSR activities and hence are less intended to commit corporate frauds.

### FRAUD SCANDALS OF THE EARLY 2000s

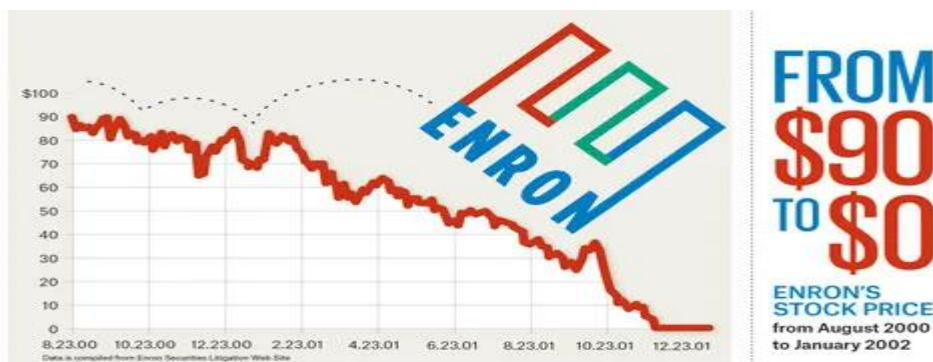
#### Enron

Due to facing pressure from shareholders, the executives in the Enron company started getting involved in illicit accounting practices one of which is the “mark-to-market accounting” in order to hide the troubles. The main cause of Enron fraud was their executives pursued power, greed, profit, which emerged as cheating, lying and other forms of rule breaking activities that was against the corporate ethics of the company. The shareholders were not taken into consideration and the decisions were made on the basis of executives personal benefits. The Enron scandal was the largest business scandal in the United States, which initiated the need of having strong business ethics and corporate governance in order to avoid such fraudulent scandals to occur in future.

#### Tyco

Due to facing pressure from shareholders, the executives in the Enron company started getting involved in illicit accounting practices one of which is the “mark-to-market accounting” in order to hide the troubles. It was a theft made by the company former chairman and CEO of \$600 million from the firm.

#### World Com



The WorldCom fraud scandal was put on the light in June 2002. This happened when the audit unit of the company noticed a more the \$3.8 billion fraudulent entries on balance sheets. The company had over recorded its assets with more than \$11 billion.

#### Health South

The executives at HealthSouth, made sure that their financial statements were able to meet analyst expectations, the managers fixed the earnings if they seemed short in order to manipulate the results, false documents were also created to hide any fraudulent statements.

#### Impacts of the fraud scandals

The fraud scandals caused significant losses to the shareholders, employees and the creditors of the fraud targeted companies and with that the fraud also impacted the proper functioning of the capital market (Carroll,1979). This also raised a concern of having strong and effective regulations and corporate culture that is aimed at limiting the consequences of fraud occurrences in future. To achieve this aim, President Bush has authorized and supported measured regulatory and enforced strong responses to avoid such scandals by making due concentration is made on two governments and regulatory actions.

#### Increased government regulations

The enforcement of Sarbanes Oxley legislation was a great step to promote transparency and bringing greater accuracy in the financial information. With that the measure of developing provisions to promote auditor and director independence and also to promote the tightening of internal controls to avoid the intended fraudulent to manipulate the company accounts and information. The measured regulatory framework is aimed to add transparency and uniform and accurate information flow to the stakeholders and investors. Therefore the Section 406 of the Sarbanes Oxley Act and the implementing rules of the SEC has created tough regulations for the corporation to manage the fraudulent activities.

### Oversight of public corporations, boards and the audit profession

The Public Company Accounting Oversight Board is created in 2002 by the Sarbanes Oxley Act to regulate and oversee the audits of the public companies and other issuers to protect the investor's interest as well as public interest by minimizing the audit risk (Carroll, 1979). The board is aimed at protecting the investors and stakeholder interest by ensuring that the company financial statements are prepared

### The dimensions of a nation's culture and its effects

The dimensions of a nation's culture, also have a very big effect on how cooperations thrive in different places. For example, some advertisements by some cooperations fail to put into consideration the cultural values of a certain nation and that end up costing them a lot. The national cultural dimensions have a very real impact on the ethical behaviors and the decisions made and implemented by the corporations (Tsakumis, 2007). The factors that reveals the national culture influence on the corporate ethics or work culture are the power distance, individualism and collectivism, uncertainty avoidance, masculinity vs femininity, and orientation phenomena. The presence of these factors contributes to the ethical standards formation within different nations as the countries with positive impact on the national culture has low history of fraudulent corporate scandals.

The national culture reflects the ethical principles that give an impression of the current status and shows the ethical code of conduct on the basis of economic, ecologic, and social parameters. The Long term orientation index of the national culture has higher levels of ethical values as compared to the short term oriented countries because the higher value of time leads to better management of deadlines, employee motivation, and focused and strategic business planning (Thanetsunthorn, 2015). With that the LTO also supports the ecological perspectives by focusing on sustainability and employees well being.

The power distance index dimension reflects that the nation with low power distance are less likely to accept the inequality in power and authority are hence being less expected to agree with supervisor's decisions and promotes contradictions. The countries with low power distance, the formal code of ethics is not considered as professional norms and rules and the managers has less influence on business ethical behavior as compared to high power distance cultures. The high uncertainty avoidance is relied on the requirement of having documented code of conduct and implementation of formal ethical guidelines in order to avoid the uncertainty and doubtful situations.

Therefore the three major dimensions of assessing the national culture influence on ethical code of conduct of business are important to to analyze the corporate culture and ethical decision making and hence the national culture is considered as a pulse of the society on which the ethics were grounded and built.



The nations with high national culture and positive culture dimensions are less likely to face the fraud scandals as compare to other countries. The national culture involves the social, ethical and the ecological aspects that are required to involve sustainability in ethics and code of conduct of individuals as well as in businesses (Tsakumis, 2007).

Thus the national culture has a real influence on the business behavior and on the business ethical standards.

## WHAT CORPORATE SOCIAL RESPONSIBILITY ENCOMPASSES

### Economic expectations

The corporate social responsibility encompasses various expectations which are categorized differently. The first one is the economic expectations, it involves having business operations that aim at improving business and at the same time being involved in practices that are sustainable. The economic responsibility owes the business to society to permit them to be created and sustained. The businesses become sustainable only by being profitable, and able to incentivize the stakeholders to have adequate resources to operate efficiently. The society allows businesses to make profit by accepting their products or services to meet their needs and requirements (Thanetsunthorn, 2015). The business creates profit only when they add value to society and by fulfilling the economic responsibilities of business by meeting the economic expectations of the society and stakeholders.



### Legal expectations

The other expectation is legal expectations. This is where the cooperation is expected to do business while following and obeying the law. The legal expectations are the grounded guidelines and regulations on which the society allows the businesses to operate and function. These legal rules include the laws and regulations that reflect the society's view of codified ethics that are intended to govern the business to articulate the notion of having fair business practices (Tsakumis, 2007). The legal responsibilities are meant to guide businesses to perform consistent with the expectations of the government and law. They are also meant to comply business practices with the various federal, state and local regulations. The legal aspects and expectations motivates businesses to fulfill all their legal obligations to society and provides goods and services meets all the legal requirements to avoid disputes and frauds to exist.

### Ethical expectations

The ethical expectation involves having fair practices when it comes to labor and practices of trade that are equal. Apart from the economic and legal parameters, the society expects businesses to operate their activities in an ethical manner by embracing their activities, norms, standards, and laws of doing business (Thanetsunthorn, 2015). The ethical expectations aim businesses to conduct their affairs in a fair and objective manner, even though in situations where law do not provide guidance or dictate any possible courses of action. In order to make businesses responsible for their working and code of conducting business, the involvement of ethical expectations and responsibilities are must to protect the stakeholders' moral rights. The ethical responsibilities prevent ethical norms from being compromised and promoting good corporate governance by functioning in an ethical and moral way.

### Philanthropic expectations

The philanthropic expectation involves practices such as providing funds for programs that are educational, being in the forefront of supporting health initiatives, being donors to various projects, etc. therefore the philanthropic expectations involves all forms of business giving by embracing businesses voluntary or discretionary activities. In today's world, the philanthropic expectations play a vital role in everyday expectations of the public and help the society and individual to relate with the company efforts (Ethics Unwrapped, 2017). The philanthropic activities are mainly voluntary and discretionary to company affairs and are not mandated by the law. Perhaps in order to manage the balance between the economic and nature aspects, the philanthropic activities help companies to overcome the losses caused to the nature in order to meet the economic requirements of the business by involving in some good efforts to save the environment and the



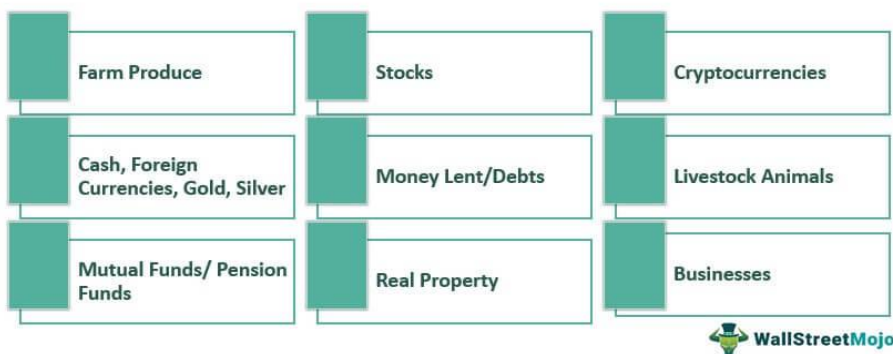
common good of the society. To fulfill this perceived business requirement, the companies are engaging in a variety of activities like donations, gifts, environment focused business activities, causing low pollution, implementing technologies that cause less harm to the environment, saving water and electricity and confronting towards low waste business ideas.

The four elements and expectations of the corporate social responsibility forms a conceptual framework that is based on the economic, legal, ethical and philanthropic responsibilities that businesses need to fulfill in order to manage the societal image and acceptance to operate effectively (Tsakumis, 2007). Among the four responsibilities, the economic and the legal aspects are the required aspects of the business to operate while the ethical and the philanthropic parameters are desired and expected by the society.

### Elements of Zakat and taxation

Zakat is a part of wealth that involves having an owner of a bank give by compulsion to the rightful receivers following specific requirements, mostly done by Muslims. It is a specific percentage which is 2.5% of the net income (alothricpa.com, 2021). The Zakat is aimed to bring purification by obliging Muslims to pay a certain amount of money at the end of the year to the needy people who can no longer work and provide for themselves. Zakat is one of the five fundamental pillars of the Islam and pose greater importance in Islamic countries. The Zakat is positively related to the corporate social responsibility of the businesses as it is intended to help the needy people and to do good to the society by spending their extra income or profits on good cause and hence considered as the best way to pay back to society in an effective way. The Zakat in Islamic nations are meant to circulate the wealth in society and also helps in minimizing the gap between the different classes of the society by transferring the extra wealth to the needy class (alothricpa.com, 2021). Therefore Zakat is an important element in the Islamic concept of justice that implies caring for all members of the society and has clear implications for business practices.

## Zakat Eligible Properties



Hence, it results in economic prosperity by transferring wealth from those who have surplus to the poor and helps in improving the poor's purchasing power which lead to higher demand of goods and economic growth. Zakat however, helps narrow the gap between the rich and the poor. Corporate taxes are usually higher compared to Zakat. Taxation is the sum of money to be paid by the people or businesses to the government for public purposes and hence considered as an obligation imposed by the state on the citizens. The main purposes of imposing taxation is the redistribution of labor, reduction in inequality of income, and to make people to contribute to government administrative activities and to contribute to the government sources to meet the state expenditures (alothricpa.com, 2021). The modern taxation is more strict and higher as compared to the Islamic Zakat system, but the Zakat is an important element of the Islamic countries and carries religious and ethical codes to share the resources in an effective way. The taxation in every country is decided or imposed according to the type of national culture and corporate social responsibility involvement.

## CONCLUSION

The relationship between the dimensions of a nation's culture and how corporations engage in social responsibility and the relating taxing outcomes. The national culture has its influence on every aspect of corporate codes of conduct as it reflects the ethics, behavior, and the other important aspects of decision making that enable the country to establish their own codes of conduct (Ethics Unwrapped, 2017). The national culture is therefore considered as a pulse of the society which become the root cause of every outcome as the human learn from their surroundings that consist of rules, customs, skills, and values

that aid them to participate in society and act accordingly. There are some national culture parameters that define the value of ethics imparted among people and the level of opportunity possess them to perform their ethical choices. Therefore the national culture has a great impact over the business ethics and thus have a significant impact on doing business with different organization around the world.

Corporate social responsibility associates negatively with corporate tax payment. In most firms, they act as substitutes for each other. Also, if the two work hand in hand in most firm, it is realized that corporations that appear responsible, socially more often than not get to pay less tax. Tax is a return which is due on investment made by the society from which the companies usually benefits. Hence tax is due to the state in which the company operates and generates profits in order to relocate the profit for taxing purposes. The corporate social responsibility is in the interest of both the company and society as it entails the competitiveness of the companies by addressing their social responsibilities. This help companies to build long term employee, customer as well as investors trust by presenting them the sustainable business model by identifying and preventing the possible adverse impact of the business on the environment and community. The corporate social responsibility is hence seen to set the limits on the requirements for the tax planning activities due to the fact that the corporate tax panning is appropriate and necessary, but it is also ascertained that the some aspects of tax planning is inappropriate from the shareholders point of view and thus do not entail any specific attention and concern.

The taxation policies differ in every country as it is related to the national culture present in countries like in Islamic countries the taxation is mainly charged through the Zakat system while in other countries the taxations charged on the basis of their related culture and taxation policies (Ethics Unwrapped, 2017). The taxation policies are important to implement in order to maintain the growth and progress of the country and to entail the redistribution of wealth among the nation and with this intention, every country has its own set of regulations and policies to implement appropriate taxation laws that are enforced throughout the nation and need to be followed and paid by every business organization.

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