# COMMENTARY

## Arthur Wyatt on International Accounting Standards: A New Perspective

Until recently international accounting standards published by the International Accounting Standards Committee have been little more than a curiosity, at least in the United States (although the moral support of the SEC in the early 1970s was beneficial to its credibility). That perspective is likely to change rather dramatically in the 1990s, with significant ramifications for academics, multinational entity preparers, securities regulators, investors and their advisers, and even for national standard setters. We all can benefit from a deeper understanding of the rather dramatic changes that have led to a shifting focus in the international arena in the evolution of accounting standards.

Those with primary interests in the United States' standard setting scene probably feel oppressed in at least two ways as the 1980s draw to a close: (1) the obsession of the Financial Accounting Standards Board with excruciatingly detailed standards (followed by even more detailed interpretations, explanations—and, in some cases, amendments) and (2) the heightened controversy over the process of standard setting, over whether standards should be logically derived by a board of independent individuals with expertise in accounting or be politically driven based upon which power groups can command the greatest influence over the standard setters during the process of standards development.

As the 1980s progressed the FASB seemed to be increasingly beset as each sensitive standard was adopted. Statement 87 (pensions) reflected more the effects of preparer initiatives than of logical analysis. Statement 96 (income taxes) was markedly more logical and conceptually tight, but led to broadly-based dissatisfaction and virtually instant reconsideration in Board deliberations even before it became effective. The outlook for the standards on postretirement benefits and financial instruments is more of the same—confrontation between those who believe standards must meet certain minimum standards of logic, cohesiveness and neutrality and those who believe standards must be "practical," i.e., must reflect the objectives of those who are the most effective lobbyists as the standard setting process unfolds.

Until now, at least, the international standard setting scene has avoided both of these potentially damaging phenomena. International standards have been crafted in broad terms and often with two (or more) acceptable alternatives. Even if entities in the United States had been required to adhere to the standards, few would have objected for practical reasons (although loss of control over standard setting would have offended some). The standards simply were not definitive or detailed enough to cause problems in application in practice in the United States, given the level of detail and specificity we have become accustomed to in our standards. Probably for this reason, among others, IASC has largely avoided the negative aspects of lobbying and interference that continues to plague the FASB. As noted earlier the IASC standards have been largely a curiosity, not a phenomenon to be taken seriously. But, this is likely to change.

### HOW IASC OPERATES

IASC represents more than 95 accountancy organizations worldwide. It complements the role of the International Federation of Accountants (IFAC), which coordinates the professional activities of accountancy bodies worldwide. IFAC recognizes IASC as the sole body with authority to issue International Accounting Standards.

The IASC currently has 14 members representing 13 countries and the International Coordinating Committee of Financial Analysts Associations. Each member is entitled to two representatives but only one vote. Members are nominated by the IFAC council in consultation with IASC. Prior to 1988 each founding member of IFAC was a member of IASC, but in 1988 that notion of permanent membership was discontinued. The United States representatives are nominated by the AICPA and NAA.

IASC has a Secretariat that provides staff support to the Board and its committees. It carries out research, assists with the promotion of the use of the standards, and provides liaison with the accountancy profession, national standard setting bodies and the users and preparers of financial statements. Funding is provided by member countries, by IFAC, and by the sale of publications. The annual budget of IASC is approximately $650,000.

The IASC Board meets for a three-day period five times in each two-year period, with most meetings preceded by a one-day meeting with the broadly-based IASC Consultative Group. Projects are assigned to steering committees of, generally, representatives of three to five countries, not all of which need be represented on the IASC Board. These committees develop proposals that are considered at board meetings and result in exposure drafts. Comments received are considered by the steering committee, and it prepares a revised draft of a standard for Board consideration. Most projects require a minimum of three years from formation of the steering committee to issuance of a standard.

While due process procedures are followed in release of an exposure draft, with a period of six to nine months common for responses, IASC does not hold public hearings nor are its deliberative meetings open to the public. In fact, in operation the IASC is much like the Accounting Principles Board was during 1958-1973 in the U.S. Board deliberations on a topic on the first day of a meeting result in suggested changes. The staff prepares a new draft overnight that is the basis of discussion the following day. A new draft emerges that night and becomes the basis for the final day of discussion. With good fortune, remaining contentious issues are resolved on that day and provide the basis for an exposure draft, a document for discussion at the following meeting, or approval as a standard.

## THE OBJECTIVES OF IASC

The objectives perceived for IASC upon its formation in 1973 included increased harmonization of accounting standards among countries, development of a basis for underdeveloped countries to follow as an accounting profession emerged in those countries, and increased focus on accounting and reporting responsibilities of multinational companies. In spite of criticisms that IASC objectives are misguided or that harmonization is an impossible (even unjustified) goal given cultural, legal and socioeconomic differences among countries, IASC has achieved some modest progress.

Simply getting accounting professionals from different cultures together to discuss accounting and reporting issues of mutual concern has some benefit, even if it is only to enhance understanding among the participants. Progress in articulating standards to guide technical decisions is a necessary first step to improve harmonization and to guide accounting decisions in developing countries.

It is in the multinational company arena, however, that the greatest, and maybe most unexpected, impetus to the work of IASC has come. The rapid growth in international capital markets, cross-border mergers and acquisitions, and generally heightened level of international commerce emerging in the mid-1980s created pressures for harmonization of accounting standards far beyond those contemplated at the formation of IASC. What started out to be a rather high-level philosophical objective has now become a market-driven necessity if international business is to achieve a level of efficiency and freedom from artificial impediments comparable to that found within the national economies of many developed countries. Harmonization is no longer merely a philosophical notion about which to argue; rather, it is a necessary ingredient to achieve the objectives of freer trade and commerce in a world economy.

## IASC MOVES TO INCREASE COMPARABILITY

The emergence of significant cross-border financings, and the consequent interest of various national securities regulators, has created within IASC an enhanced sense of mission and direction. A recently formed international organization of securities regulators (The International Organization of Securities Commissions, or IOSCO) has expressed increasing interest in the work of IASC. That interest has been manifested by participation in the IASC Consultative Group, participation in steering committees of IASC that are working to reduce the range of acceptable alternatives in existing international standards, and encouragement of IASC to develop standards in new areas: financial instruments, intangibles and cash flow statements. Assuming that cross-border financings do not disappear, IOSCO is likely to be an increasingly significant influence on the work of IASC.

In addition, IOSCO has provided IASC with both encouragement and technical advice in its most important project to date, the project to eliminate from existing international accounting standards as many acceptable alternatives as possible. This project will likely come to be seen as the watershed event in the history of IASC. The expectation is that IASC will adopt a standard in 1990 to eliminate from acceptability more than 20 currently acceptable alternatives. For those areas in which alternatives will remain, one method will be identified as preferable. If the alternative to it is followed, the reportng entity will be required to provide information in the footnotes to reconcile to what the results would have been had the preferable alternative been adopted. The incentives to undertake this project were numerous, but the prodding and support of securities regulators was very significant.

These developments should really surprise no one. In the United States, formal standard setting in accounting did not emerge until after creation of the Securities and Exchange Commission. National standards development in many other countries has followed the development of capital markets and of securities regulators assigned the responsibility for enhancing fairness in the operation of those markets. More recently, securities commissioners in many countries have come to recognize the improved efficiencies that would flow from elimination of accounting differences across countries. Many believe that markets extract a price for these inefficiencies and that, therefore, financing costs would decline as inefficiencies related to accounting differences are eliminated.

Many will continue to argue the propriety of attempting to achieve greater harmony among accounting standards found in many national economies. Change, sometimes rather dramatic change, is necessary to achieve greater harmonization. In the absence of economic incentives, effecting such changes that would override long-standing customs and, in some cases, run counter to a national culture was admittedly a long-term project of questionable success, and thus arguably a project of questionable merit. With the emergence of economic incentives, however, and particularly the remarkable progress in Europe within the European Communities to reduce differences among a wide variety of national policies, accounting harmonization takes on quite a different perspective. Instead of being primarily a philosophical exercise, harmonization of accounting standards has become a key ingredient in fostering efficiency in the phenomenon of high volume cross-border finance, a phenomenon that gives every sign of accelerating rather than becoming merely an aberration of the 1980s. Harmonization of accounting standards is critical to creating comparable data on which to base decisions and to enhancing the credibility of those data for use across borders.

## IASC STANDARDS: A NEW PERSPECTIVE

What is the outlook, then, for achieving increased harmonization of accounting standards? Given the problems that the FASB (and its predecessors) have had in the United States, and similar problems in many other Anglo-Saxon countries today, is it reasonble to expect any real payoff from efforts to increase harmonization in accounting standards? Or, are IASC efforts fruitless and doomed to achieving little, if any, success?

While definitive answers to these questions await the future, the fact is IASC does have a window of opportunity in which substantial progress seems possible. The convergence of several powerful forces opens that window and provides real encouragement to those who believe sound and credible (true and fair) financial information is essential to achieving the benefits of a world economy characterized by relative freedom from national constraints on trade.

Those forces include: increased cross-border financing; emergence of true multinational companies; a heightened willingness to cooperate across borders (e.g., the European Communities) to enhance national, regional and even global economic strength; an awareness by securities regulators around the world of the necessity for comparable and credible data; and a vehicle, IASC, to articulate standards that can move us closer to the level of comparable and credible data that a free world economy requires.

Accounting standard setting is an evolving process, one that has been characterized both by substantial improvement and by false starts and even fruitless side trips. Evolving processes often produce such mixed results. Evolving processes also often achieve progress in bursts when conditions happen to be most favorable. Market forces have provided an impetus to accounting standards harmonization today. Whether international accounting standard setters can capitalize on this opportunity may well determine the significance of financial information in the world economy of tomorrow, which in turn, may positively impact the efficient allocation of capital for the benefit of all.