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IASC:Obstacles and opportunities (Address American Accounting Association Chicago, meeting, August 7, 1981)

Composition and objectives of IASC

The International Accounting Standards Committee was established in 1973 by the professional accountancy bodies in 9 countries. It was set up, because clearly there was a need for international standards, but apparently nobody cared to sit down and do something about it. Since then, bodies from about 40 other countries have applied for membership, and by now IASC comprises in its constituency virtually all of the worldwide profession, to the extent it has been organised nationally in private bodies. Governments and governmental audit institutions are not entitled to membership. This explains why from the 180 nations or so that exist in the world less than 50 are represented in IASC.

The objectives of IASC are to improve and to harmonise company reporting around the world. If we restricted ourselves to harmonisation only, the ultimate result would be the phrasing of common denominators: those elements that are already common to financial reporting in all countries. Such an exercise would *degrade*, instead of *upgrade* the quality of financial statements. Only by marrying the objective of harmonisation with that of improvement have we set goals that are worthwhile to pursue.

IASC is a private sector professional exercise. It is meant to remain that way. Not because we feel that others should not be allowed to have a say in standardsetting; on the contrary, we feel that they too should be involved. But it is our experience that only in the profession is there a sufficient body of common knowledge, expertise, independence and mutual understanding - all essential ingredients to achieve our goal: unbiased, workable standards that contribute to improved reliability and understandability of financial statements, worldwide.

From the start, IASC was meant to be a truly international exercise. There was, and there is, no intention to copy the standards elaborated in countries with long and profound experience in this field, such as U.S. or Canada. Mainly for two reasons:

- an emotional one: in many countries the adoption of foreign rules is considered as an infringement on their sovereignty, that casts doubt on their own ability;
- a rational one: national standards are tailored after national needs and

national business-environments. But in other countries those needs and environments are not necessarily identical.

Therefore, in developing a standard we basically start from scratch, seeking input from all our members. Of course, the material elaborated in the advanced countries is studied carefully, but the views expressed in those documents are not decisive for us.

The first priority for IASC was to produce a stock in trade. The next priority is to sell our merchandise, i.e. to seek adoption and compliance. Let us examine what obstacles are encountered in these two fields.

Obstacles in the development of standards

The main obstacles in developing international accounting standards are, according to my experience:

1. A provincial outlook, held in various nations. As long as people are convinced in advance that their own views are superior to those of others, known or unknown, it is hardly possible to reach agreement on a common solution. Although this provincialism is absent amongst the Board members, it is present very often with their constituencies. And it is amazing to observe, that countries in which accounting is most developed, are least of all inclined to listen to others. Amazing because one would expect that highly developed countries would be well aware of the conceptual and practical weaknesses, that are characteristic of today's imperfect state of the art. I am afraid the USA are no exception in this respect.

I recognise that the language barrier is a serious obstacle in the exchange of views. It is my impression that on the continent of Europe there is more knowledge about Anglo-Saxon literature than there is the other way round. I think that is a pity.

In order to avoid any misunderstanding, I wish to add that I have discovered no provincial attitude with your FASB or your AcSEC. These gentlemen are very much aware of what is going on internationally. But they have to reckon with their constituencies, the majority of which apparently feel that in accounting, life is already difficult enough without international entanglements.

2. A second obstacle is presented by the differences in economic and social environment, in which accounting has a role to play. In different countries there is a different view on what is, or should be, the primary purpose of financial statements. In some countries, and the US is one of them, the investor and his decisions are considered to be most important. In others, such as the UK, it is the shareholder. In still others, such as Germany, it is the creditor. In France, the information needs of Government play a major role. In some countries it is believed companies have a public accountability to a great variety of stakeholders. These differences in purposes which are in the minds of accountants lead to different views on what is appropriate accounting treatment. Some operate from an environment of extreme conservatism, others from an environment that borders on creative accounting.

Apart from that: the impact of certain economic phenomena may vary strongly from one country to another. The issue of foreign exchange gains and losses is quite different depending on whether your reporting currency is strong and stable, or weak and rapidly depreciating. Many other examples exist - in the field of interest, deferred taxation, or pension plans, to name but a few.

3. A third obstacle is presented by the fact that at the present time, there are wide divergences in worldwide accounting practices. Each practice may be well founded, and well understood in the national environment. Obviously, it is the task of IASC to try and narrow these areas of divergence. However, we have to be realistic. No useful purpose would be served if IASC were to develop standards that represented the single ideal treatment. Apart from the fact that it would not be easy to reach agreement on what that ideal treatment would be, nobody would take notice of such a standard.

IASC is operating in a field of tension between ideals and practicality. The road of many miles must be walked step by step, first outlawing practices that are clearly misleading or allow management too much latitude; next trying to eliminate options that do not contribute to fairness in reporting.

This is not to say that we want to get rid of all options. Rather, we feel that we should first try and define under what circumstances what option is appropriate. Conditions and transactions may be identical in form, but may vary in substance.

4. Several obstacles met in the process of setting international standards are the same that give headaches to national standardsetters. Economic phenomena may be considered from different angles, leading to different treatments. The objectives of financial statements are often confused. Interest groups may exert pressure to move you into one direction or another. Standards do not, and cannot, cover all questions arising in specific industries or in specific circumstances. These obstacles will remain as long as accounting is an imperfect art, which I am afraid will continue to be the case for some time.

Obstacles in enforcement

Next, let us examine what obstacles have to be overcome in order to achieve adoption of and compliance with International Accounting Standards.

1. The most formidable obstacle is raised by tax laws. In many countries in the world enterprises are required to draw up one set of financial statements only, serving both tax purposes and reporting purposes. Since the Revenue Service has an overriding interest in profit as computed for fiscal purposes, tax laws often prescribe in detail how profit should be measured, and Tax Courts render verdicts how these regulations should be applied. In this framework it is unavoidable that business is more concerned about tax saving than it is about proper and honest reporting. And equally unavoidable is the consequence that International Accounting Standards are judged primarily by these tax implications, the Revenue Service opposing

standards that would reduce profits, and business opposing standards that would boost profits.

But even in countries where separate sets of financial statements are allowed for tax purposes and for reporting purposes it often happens that Government makes available certain tax reliefs on the condition that the items concerned are stated in the reports accordingly. We have seen this at various times with regard to LIFO valuation, accelerated depreciation and capitalisation of interest cost.

Clearly, we cannot hope for improvement and harmonisation of financial statements unless all ties between tax accounting and reporting to the public are cut completely. This would be the single most important contribution that Governments are able to provide to the cause of international harmonisation.

2. A second obstacle is, again, the law - not the tax law this time, but laws regulating reports to shareholders and the public. In some countries, this law goes into great detail, both on disclosure and on measurement. In this framework, the notion of 'true and fair view' loses importance and the primary objective of preparers and auditors is compliance with law and regulations. And people are led to believe that the law, although maybe not ensuring superior reporting, at any rate ensures reliable and comparable reporting. One might query both.

For IASC, this situation means that in such a country International Accounting Standards will not be adopted unless they are incorporated in the law.

Now, changing the laws is a tiresome and time-consuming task. In most countries lawmakers are not leaping to their feet to do this job, because company reporting is not a hot political issue. And if it is, even worse, because then politicians will handle the issue with strong political overtones.

3. A third obstacle may evolve from the activities of the national standard setting bodies. In more and more countries the need is felt to set accounting standards, and a body is established, either by the profession or jointly by a number of interested parties, to do this job.

There is a tendency with these bodies to address more and more subjects, to give rules in more and more detail, and to leave less and less options. Seen on the national level, this may have merits. But seen from an international viewpoint, problems arise. If many countries have detailed rules on many subjects, there is bound to arise an incompatibility or even conflict between these national systems. This is unfortunate for international enterprises who address their reports to readers both at home and abroad, and it reduces the credibility of their statements abroad.

At the same time, once there are national standards, it appears to be rather difficult to adapt them to international consensus. As soon as there is a national standard, national positions become entrenched, and it is hard to exchange that position for one that is considered as second rate. Apart from that, national standardsetters are bound to rules of due process, and they have to weigh carefully the feelings voiced by their own constituency. That

means that often they are unable to compromise even if they would wish to do so.

4. A fourth obstacle is the potential competition between international standardsetters. As you all know, apart from IASC, the UN and the OECD are now engaged in the field of company reporting, especially by multinational enterprises. OECD has made it clear that it does not want to go into the setting of standards, but wishes to restrict itself to clarifying the Guidelines for disclosure of information, and to energising in some way or other the process of international harmonisation. In the UN, on the other hand, it is quite clear that a number of countries wish the UN to develop and issue enforceable standards for reporting by multinationals. It stands to reason that if it comes to that, there is a serious danger of incompatible and conflicting sets of international standards; the more so since the UN exercise has strong political overtones. The fundamental debate is not on what constitutes proper company reporting, but on what information should be made available to host countries, especially developing ones.

5. Last but not least: the addressees of standards, business. They are the people asked to comply with International Accounting Standards, and if they do not, they are an obstacle in getting compliance. Amongst the enterprises that are reluctant to formally adopt International Accounting Standards, two broad categories can be distinguished:

- those whose affairs are purely domestic, and that hold the view that international standards are none of their business. The vast majority of companies, in the USA and elsewhere, belong to this category;
- those whose affairs are international, that recognise there is a need for international harmonisation, but are hesitant to back IASC as long as they are not sure IASC is a winning horse.

On the other hand, it should be noted that many companies do comply with International Accounting Standards for the simple reason that these do not require anything that is not already in their national standards.

Progress made

So much about obstacles. Has IASC, notwithstanding these obstacles, made any progress? I believe it has.

In the field of developing statements, IASC has approved 15 standards and 7 exposure drafts. Some documents cover some quite sophisticated subjects, such as leases, pension costs and reporting by segments.

What about adoption and compliance? It is clear today, that the original idea in IASC, to enforce compliance through the auditors, does not work satisfactorily. Apparently, the worldwide profession lacks the power to enforce compliance. Nevertheless, International Accounting Standards do not go unnoticed.

Some countries, such as Malaysia or Nigeria, who have no standard-setting resources of themselves, adopt all International Accounting Standards, lock

stock and barrel, as national ones. In other countries, such as the Netherlands and the UK, the national standard-setting body carefully studies every exposure draft and sends in its comments. And subsequently they try to incorporate, to the extent possible, the contents of International Accounting Standards into their national standards.

In still other countries, where the Government has a dominant influence on company reporting, such as France and Japan, there is a growing awareness on the part of Government officials, that national requirements are less than perfect, and are due for revision. There is an awareness too that it is beneficial to the international flow of capital, and in that way to the national economy, that companies should be permitted to report in compliance with worldwide requirements. International Accounting Standards, therefore, are studied, and their inclusion in national regulations is contemplated. Of course, this process will take time, but slowly the message comes across.

Progress is made too in a growing willingness on the part of international organisations of users and preparers of financial statements to become involved in the work of IASC. Recent contacts with international organisations have resulted in the decision to form a consultative group in which stock exchanges, financial analysts, business, financial executives, labour, the World Bank and intergovernmental bodies will be represented. This involvement of interested groups in the process of setting international standards of course does not mean that they will endorse individual standards. But it does prove that they consider IASC's efforts as worthwhile and promising.

The future

I expect that in the near future, the emphasis of IASC - apart from the continuing process of publishing standards - will be on two major tasks.

The first is to promote *implementation* of international accounting standards. To that end, we continue to need the support of the profession. But that support alone is not enough. We need the support of all interested parties, and we have to find ways and means of gaining that support.

Recently, we approached prominent companies in some board member countries suggesting that they should make reference to International Accounting Standards in their financial statements, for example by saying: 'These statements have been prepared in accordance with generally accepted accounting principles in country X, which conform in all material respects with International Accounting Standards'.

Another method we are using is to encourage our member bodies to urge their national standard-setters to phrase or rephrase their rules in such a way that they are in line with International Accounting Standards. National rules may go into more detail, but they should not require a treatment that is rejected in an International Accounting Standard; they should not require less than International Accounting Standards do.

A third item that may have a favourable effect is an offer of assistance that we have made to the OECD and the UN, in order to ensure that statements of

these bodies are workable and compatible with International Accounting Standard. We hope they will reach the conclusion that by encouraging the adoption of an International Accounting Standard, they would promote adequate reporting without having to develop a Statement themselves.

The second task that may develop for IASC in the near future may be to act as an *honest broker* whenever serious conflicts arise or exist between the requirements of different national standard-setters. At present, there is no machinery for preventing or resolving these conflicts which are annoying to preparers and confusing to users. It is quite in line with the responsibilities undertaken by IASC to offer its good services, to become involved in task forces, to stimulate talks in order to develop common solutions.

Further down the road is looming another task. So far, International Accounting Standards have been developed on the basis of common sense, on what is good practice wherever it may be in the world. But one day we shall be nearing the end of 'rough justice' as a proper means of making standards. By then, we shall have to reconsider what we have been doing, on the basis of a more fundamental study of what accounting really is, what it should achieve, how it should be achieved. Something like a conceptual framework may become necessary, a subject your Association discussed last year.

IASC follows with great interest the efforts deployed by the FASB in order to come to grips with the fundamentals. And we hope something will emerge that is useful not only to the USA, but to other countries as well. At the same time, we recognise that developing a worldwide conceptual framework is fraught with staggering problems.

In summing up, it is my belief that IASC has no easy future. But it *has* a future. The world needs international accounting standards, applied worldwide by business, because they are beneficial for mutual understanding. The world will not rest until it gets what it wants.