

# The role and future plans of the International Accounting Standards Committee

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THEMA

## 1 Introduction

In 1972, a number of far-sighted accountants took the view that the problems of accounting should really be solved at the international level rather than the national level in order to achieve global uniformity. A start had been made with the formation of the Accountants' International Study Group in 1966, a co-operative venture of the professions in the United States, the United Kingdom and Canada. By 1972, the time was seen to be ripe for another step. At the 1972 World Congress of Accountants, held in Sydney, an agreement was made to establish the International Accounting Standards Committee and it commenced operations in 1973. Coincidentally, feeling in the United States had been growing in conviction that new institutions and approaches were needed to deal with difficult and long-running accounting issues in that country. In the same year as that in which IASC commenced operations, the US Financial Accounting Standards Board was formed to take over the setting of accounting standards from the Accounting Principles Board. 1998 saw the twenty-fifth anniversary of both IASC and FASB.

## 2 The Constitution of IASC

IASC was originally established as an independent organisation, the members of which were those professional bodies which were parties to the original agreement. It is still independent as far as decision-making is concerned: standards are approved by the Board of

IASC and are not subject to confirmation by any other body. However, in 1983, IASC joined forces with the International Federation of Accountants (IFAC). The effect of this arrangement was that the members of IFAC became the members of IASC. These members are the professional accounting bodies from around the world, in round numbers about 140 professional bodies from over 100 different countries. At the present time, the IASC Board comprises up to 13 country members and up to 4 additional co-opted members.

## 3 Due Process

IASC develops its standards in accordance with procedural rules. A steering committee is formed to develop proposals for each technical matter on the Board's agenda. The steering committee is usually chaired by a member of the Board and it works with a project manager from the IASC staff to agree on the research required and prepare draft documents. The steering committee publishes a draft Statement of Principles for public comment on its main projects. This is the basis for the Board's settling a Statement of Principles, which is not formally published but is made available if requested, and subsequently an Exposure Draft, which is published for public comment. Exposure Drafts must be approved for publication by two thirds of Board members and finalised Standards must be approved by three quarters of Board members. This means that we impose the rigorous requirement of obtaining twelve positive votes for a Standard out of the present Board membership of sixteen. The Board normally meets three times per year for about three days at a time. However

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because of the urgency of its work program, the Board met four times in 1997 and, in 1998, five times for a total of 25 days. On this basis, the procedures required for agreeing a major Standard can be completed in the most favourable circumstances in about two years.

Another important step, relating to due process, was taken in November 1998, when the Board decided to open technical discussions at Board meetings to public observation, beginning in March 1999. The arrangements are explained on IASC's Website (<http://www.iasc.org.uk>). Members of the public can now follow the progress of projects and make written representations to the Board about them; they can also observe the quality of the technical discussion and the way in which decisions are made.

#### **4 IASC's Achievements**

This paper next comments on some of the achievements of the Board in its twenty-five years of life. Originally, the objective of the Board was to produce 'basic standards'. This, no doubt, reflected the view that it would be easier to reach agreement on basic standards than on highly detailed standards and it addressed the wish to have standards that would be readily usable in developing countries as well as improving the level of harmonisation among the richer countries of the world. Early standards often allowed alternative treatments to accommodate the different approaches adopted by major national standard setters.

Today we give importance to providing standards that will bring greater uniformity to accounting reports of multinational companies, particularly those with stock market quotations, but we continue also to wish to have our standards used in developing countries. A number of countries, some relatively wealthy and others relatively poor, take international standards as the basis for local standards, issuing them locally with little or no amendment. However, the idea that we could restrict our standards to basic matters has long since been abandoned. As the world develops more and more complex contractual arrangements, including financial instruments, genuine uniformity in global accounting calls for more extensive and sophisticated standards.

IASC has also recognised the need to reduce alternatives wherever possible. Allowing alternatives can work against real harmonisation. Their elimination can cause pain to businesses which have become accustomed to the flexibility provided by alternative treatments but the IASC Board has been able to make a good deal of progress in eliminating alternatives, particularly in its omnibus project on Improvements and Comparability, completed in 1993, and in more recent major revisions of standards such as the one on income taxes. IASC has issued 39 International Accounting Standards, one or two of which have been superseded and several of which have been revised. It also has a framework document which deals with the objectives of financial reporting and definitions of the qualities required in financial reporting and the elements of financial statements. Its framework document is similar to corresponding statements of the national standard setters.

An organisation like IASC must give a good deal of attention to the means by which it encourages use of its pronouncements. An international organisation of its type cannot rely on direct legal backing and it must look for other means. The Member Bodies of IASC undertake to promote the use of international standards in the countries where they operate. Recommendations of professional accounting bodies can be highly influential and this is particularly the case when international standards are converted into local standards whether or not they have the force of law.

#### **5 The IOSCO Agreement**

Acceptance of international standards for financial reporting connected with stock exchange listings is another important way for IASC to make progress. Our standards are already accepted by many stock exchanges, the London Stock Exchange having led the way soon after the foundation of IASC. However, the regulatory arrangements in Canada and the United States still do not permit the use of international standards for stock exchange purposes, even for the limited purpose of cross-border listings. For some time up to 1995, IASC held discussions with the International Organization of Securities Commissions (IOSCO) to explore the possibility that IOSCO might endorse our standards and thereby

give some additional impetus to movements towards their wider acceptance.

A past Chairman of IASC, Eiichi Shiratori from Japan, who sadly died early in 1998, pressed strongly for IOSCO endorsement of our standards as they stood at the time. However, some members of IOSCO took the view that endorsement should be withheld until we had completed a core set of standards, a set which dealt comprehensively with the main financial reporting issues of the day. In 1995, IASC decided to accept the need to complete a core set of standards before endorsement could be expected. Completion of this core set was a desirable objective for IASC in any event and acceptance of this objective enabled us to make a good agreement with IOSCO, in which we undertook to co-operate with each other in seeking to complete the core set of standards as effectively and quickly as possible, and in which IOSCO expressed warm support for our objectives. IASC and IOSCO published this agreement in July 1995. It focused on a work programme which would be completed in mid-1999 and which covered all the areas which IOSCO saw as needing attention for IASC to have completed its core set of standards. The agreement with IOSCO said that the completion of the work programme would clear the way for IOSCO endorsement of our standards.

During the first few weeks of 1996, several of the key members of IOSCO asked IASC to consider accelerating its work programme. The need for a body of standards that could be used universally in cross-border offerings and listings was urgent. Companies wishing to raise capital on international stock markets in the near future wanted to do so without incurring the costs of preparing a new set of accounts and without delay. The capital markets wanted to enjoy the benefits of removing some of the friction affecting their competition. So IASC reassessed its work programme and at the March 1996 Board meeting agreed to adopt fast track procedures which could lead to completion of the core set of standards at its meeting in March or April 1998. The precise decision of the Board was that fast track procedures should be adopted and that the staff should proceed with the accelerated work programme as resources permit.

After the Board made its decision, the SEC, a key institution because of its role as securities regulator in the United States, issued a statement welcoming the acceleration of the work programme. It also said: 'The Commission is committed to working with its securities regulatory colleagues, through IOSCO, and with IASC to provide the necessary input to achieve the goal of establishing a comprehensive set of International Accounting Standards.' The statement of the Commission emphasised three key elements to our programme and the Commission's acceptance of its results. It was that IASC must complete the core set of standards, do so with work of high quality, achieving comparability and transparency, and that the standards must be rigorously interpreted and applied. The SEC concluded its statement by saying that when IASC had achieved these goals, it was the intention of the Commission to consider allowing the utilisation of the resulting standards by foreign issuers offering securities in the United States.

Further support for international accounting harmonisation came from the US Congress. In October 1996, Congress passed legislation calling on the SEC to enhance its vigorous support for the development of high quality International Accounting Standards. The SEC was required to report to Congress on progress by October 1997. In its report, it described the IOSCO/IASC Agreement and the considerable resources being devoted by the SEC to the project. It said, encouragingly: 'At this point, it is not clear what the Commission's final decision regarding the core standards project will be. Nevertheless, the IASC's efforts to date already have contributed significantly to raising the level of accounting standards world-wide and reducing the number of differences between international standards and accounting principles used in the United States. These and other efforts at the international level are encouraging development of accounting principles that have the needs of investors and capital markets as their primary focus.'

Interesting evidence of IOSCO's pursuit of the objective of international harmonisation was seen recently in proposals for harmonisation of prospectus requirements. At present, if a company wishes to offer its shares in, for example, London, New York and Tokyo, it must produce three

significantly different prospectuses. Work in IOSCO is aimed at allowing such a company to use just one document. In August 1997, the London Stock Exchange, in its role as regulator, issued a consultative document containing proposed rules for the non-financial disclosures in prospectuses. These rules would be for use in connection with international offerings to satisfy the domestic requirements in all major countries. The proposals were approved by IOSCO's Committees in 1998. Consideration of endorsement of IASC's standards is partly related to the wish to have a common prospectus for international offerings although it also relates to continuing listing rules.

## **6 The Current Work Programme**

The work programme agreed with IOSCO was tough and ambitious. It imposed a heavy burden on Board meetings in particular. It included a list of twelve major projects, counting intangibles, research and development and goodwill as one, some of which were revisions of existing standards rather than the preparation of completely new ones. Several of the projects involved controversial subjects. The topic of financial instruments was one where no national standard setter had a comprehensive set of requirements in operation until FASB in the United States finalised its standard on derivatives and hedging in mid-1998. The area of intangibles and related questions affecting goodwill was one in which controversies continued to loom large in the world of financial reporting. Significant and difficult issues had to be dealt with in the projects on non-wage employment costs, interim reporting, provisioning and leases. And this is not to suggest that any of the projects on the list was completely straightforward.

However, excellent progress has been made. By the end of July 1998, eleven projects in the IOSCO work programme had been completed, revisions of standards on income taxes, reporting segments, presentation of financial statements, leases and employee benefits and new standards on earnings per share, interim reporting, discontinuing operations, impairment, intangibles (including a revision of business combinations relating to goodwill) and provisions. And financial instruments, the twelfth major project, was

finished at a specially arranged extra Board meeting in December 1998. Although the date of completion of the major projects was a few months later than planned, it represented a remarkable rate of progress and was, no doubt, much earlier than would have been achieved without adoption of the ambitious accelerated work programme.

IOSCO are now finalising their analysis of the Standards in IASC's core set as preparation for consideration of their endorsement. IOSCO has a sense of urgency, which is no doubt increased by the comments of the G7 finance ministers and central bank governors, in October 1998, about action needed to bring certain Asian economies out of recession and prevent the recession spreading to the rest of the World. The finance ministers were concerned that poor accounting in the countries primarily concerned was making investors reluctant to invest and therefore raising the cost of capital in those countries. This could prolong and deepen the recession: accounting was seen as part of the economic problem. G7 called on IASC to complete its core set of standards, as it now has, and called on IOSCO to complete a timely evaluation of the standards. At their June 1999 meeting, the G7 finance ministers welcomed IASC's completion of the core set of standards and looked forward to IOSCO's completing its review. They urged all those involved in setting accounting standards to work together so that high quality accounting standards can continue to be developed and agreed internationally.

Another central area for us concerns the interpretation of International Accounting Standards. All standard setters find that their pronouncements often lead to detailed questions about application to specialised situations, sometimes involving minor extensions of the area covered by the central focus of a standard. IASC is no exception and for some time now staff have received requests for help with such matters which they deal with informally. However, as the role of International Accounting Standards grows, more difficulties may arise with aggressive interpretations of standards. For this and other reasons greater need has recently been felt for help with interpretations and a strong demand has built up for publication of formal interpretations, backed by some form of due process. Development of IASC interpretations

is important to IOSCO. Some of the national standard setters have special procedures to deal with such needs and IASC has now established similar special procedures. Lack of a procedure for interpretations by IASC might have led to the emergence of local procedures for interpretations and these might well detract from the degree of harmonisation achieved. IASC's Committee is known as the Standing Interpretations Committee (SIC). We have been fortunate in obtaining the help of a strong team of committee members. The first meeting of SIC was held in April 1997 and the first three draft interpretations were issued in August. By the end of 1998, sixteen draft interpretations had been published, fifteen had been finalised and one had been withdrawn because it was covered in the new standard on Financial Instruments. Interpretations are subject to endorsement by the IASC Board after a period of public consultation and obtaining a SIC consensus.

## **7 IASC and Europe**

IASC has an important relationship with the European Commission. In mid November 1995, the European Commission released a communication on accounting harmonisation. It said that it would ally itself more closely with the efforts being undertaken by IASC and IOSCO towards a broader international harmonisation of accounting standards. The communication was particularly notable for its recognition that only IASC is producing results which have a clear prospect of recognition within a time scale which corresponds to the urgency of the problem. The Commission would try to work more closely with IASC in the future and in particular would explore the possibility of reaching an agreed view among the representatives of member states on the Commission's 'Contact Committee' about IASC Exposure Drafts for submission to IASC.

In its November 1995 statement, the Commission said that it would examine International Accounting Standards to establish whether they contained requirements in serious conflict with the European Directives. It subsequently published a report which found only one or two minor conflicts. The Commission also noted that the Directives gave member states certain options in incorporating the accounting directives into national law. Even if no conflicts exist between International

Accounting Standards and the Directives, conflicts may exist with national laws because of the options chosen. The Commission said that it is up to member states to consider this issue and deal with it at the national level. In a speech in mid-1997, referring to developments in thinking about accounting for financial instruments, Commissioner Monti said that the Commission should consider amendments to the Directives where necessary to avoid conflicts with International Accounting Standards, provided that IASC's standards are in step with best current opinion. The Commission reaffirmed the importance of this objective several times in 1998. And IASC has reciprocated by making sure that special attention is given in its discussions to possible conflicts with the directives. These developments have brought us to the point where the Commission has developed an action plan for financial services under which it is proposed that International Accounting Standards would be allowed to be used by all listed companies in Europe as an alternative to national standards (subject to consent by each member state) and work will be started on amendment of the directives. Recently, discussion of the possibility of establishing a European Accounting Standards Board has revived although the current discussion has focused on a body which would have the function of promulgating IAS within Europe, rather than developing distinct European Standards.

These encouraging developments in thinking in Brussels have been matched by developments in France, where a new law has been passed and it has the effect that International Accounting Standards (and US GAAP, when translated in French) can be accepted for use by French companies with stock market quotations in preparing Group Accounts for domestic purposes as well as cross-border purposes. Similar laws have been passed in Austria, Belgium, Germany and Italy and are being considered by other member states of the European Union.

## **8 IASC and National Standard Setters**

Completion of our work programme in 1998 and obtaining IOSCO's endorsement has been our first objective over the last few years. This offers the prospect of securing general acceptability of International Accounting Standards for

cross-border listings on stock exchanges. However, this is only a beginning for IASC. The main goal, the objective to which all our efforts must ultimately be directed, is to bring about complete unification of the world's accounting systems: uniformity between International Accounting Standards and the national standards of all countries. We need to work with national standard setters to achieve this goal. We do not see our activity as competitive with national standard setters. We rather want to join with them in the debate about the merits of alternative solutions, taking advantage of their special position in communicating with constituencies in their own countries, so that we can move together towards agreement on preferred solutions.

A system has grown up in recent years for facilitating this co-operation. Frequent and regular meetings of standard setters are now held. IASC participates in meetings of the so-called G4 + 1, the national standard setters of the United States, Canada, Australia and the United Kingdom and Ireland, together with IASC. Other meetings of standard setters take place in small or large groups. Through these consultative arrangements, we aim to co-ordinate agendas and we also aim to try to adopt common solutions. We cannot yet be sure of our ability to agree on all the key points but at least we must make sure that each of us considers the solutions which are congenial to our colleagues. Special opportunities for progress can be created by undertaking certain projects jointly. Our work on financial instruments, for example, has been undertaken jointly with the Canadian standard setters, our work on provisions with the UK Standards Board. And our work on earnings per share and reporting the results of segments involved close liaison with national standard setters.

However, important and useful as these arrangements are, IASC believes that more needs to be done to realise the full potential of accounting harmonisation, to bring about convergence of national and international standards as quickly as possible. Several questions need to be examined. More and more countries have an interest in international accounting and perhaps more should be involved in IASC's decision making procedures. However, the Board is already a very large body for debating the complex and detailed issues

involved in setting accounting standards. Perhaps a smaller group is needed for the preparation of the proposed standards.

However it is the relationship with national standard setters which seems to be the key to the future. At present, IASC welcomes and encourages the appointment of individuals involved in national standard setting as country representatives on the Board. A number have been so appointed. And the observer membership of FASB is very helpful in providing the benefit of involvement of the World's best resourced standard setter. Yet national standard setters are not involved in IASC as fully and strongly as seems desirable. Their representation on the Board is too much a matter of chance. If convergence of standards is to be achieved, perhaps IASC should become at least partly the international organisation of national standard setters, so that national standard setters have a role in its decisions and a stake in its success. Perhaps IASC should include, as well as its present Board, a second, smaller Board of national standard setters, to prepare international standards. Perhaps the national standard setters could then make some commitment to consider the adoption of international standards as national standards, while retaining their individual sovereignty and the right to go their own way when necessary.

The IASC Board has appointed a special working party, the Strategy Working Party, to consider these issues. The Working Party published a Discussion Paper in December 1998, inviting comments on the suggestion that IASC should form a small permanent committee, the Standards Development Committee, made up mainly of representatives of national standard setters, to prepare proposed standards and submit them to the IASC Board for final approval. The Board and the Standards Development Committee would both have to approve standards before they could be published. In proposing this structure, the Working Party has recognised the remarkable success which has been achieved under present structures and kept in mind the need not to weaken the parts of the arrangements which are working well. But it has also found room for several recommendations which strengthen IASC's position for achieving its objectives in the next phase of its life.



The Working Party has also examined the need for changes in IASC's due process. When an organisation meets in private misapprehensions can develop about the nature of debates, the role of different countries and so on. The Working Party has recommended that IASC's Board should meet in public and, as noted above, the Board has decided to do so independently of the other recommendations of the Working Party. Almost certainly a number of more minor changes to due process are needed: more explanations of reasons for decisions, recording of dissents, and so on.

Comments on the Working Party's consultative document were invited by the end of April 1999. Analysis of the comment letters has shown that the details of the proposals – although not the recommendation to involve national standard setters in IASC – are quite controversial and further work by the Working Party will be needed to try to find a new structure which all major parties can agree. The Working Party will then make recommendations to the IASC Board which will decide on action in consultation with the Council of IFAC. Any constitutional changes deemed desirable could be debated at a meeting of members in May 2000 and implementation of a new structure, if one is agreed to be needed, could take place in 2001.

## **9 Where is all this work leading to?**

People at IASC are sometimes pressed with a question about where all this work on harmonisa-

tion is leading to. The objective of one uniform system of accounting throughout the world is clear. No doubt it will take a good deal of time to get there. But will there be room for several national standard setters in this world of the future or will the world have just one standard setter and will that one be IASC? This is an understandable question although asking it is a bit like asking whether we shall have world government one day. I do not think any of us at IASC are actively looking towards a time when there will be only one standard setter. The extent to which individual countries use our standards as national standards, or maintain their own procedures, is a matter for decision at the national level. As far as IASC is concerned, a co-operative relationship with national standard setters provides the best prospect for progress and changes will be considered to improve that relationship. Whatever the details of changes that are made, we shall continue to need the contribution of people who are well versed in local views about accounting and we need the help of the expertise of national standard setters more generally. Setting accounting standards is strangely complex and controversial. Good solutions are likely to come from the maintenance of several standard setting bodies who can contribute to the debate but who agree on the importance of international harmonisation.