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The Convergence Of Multinational Standards And Practices In International Financial Reporting

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ABSTRACT

The International Financial Reporting Standards (IFRS) is pending a move to incorporate a single set of accounting standards across International borders. The definitive decision for uniting the standards appears to be stalemated. The pending move by the United States to adopt financial reporting practices set forth by the IFRS to encompass a single set of reporting standards bears both advantages and disadvantages for multinational corporations. This paper examines some of the difficulties that can arise by using a single set of standards and addresses two significant studies regarding converging reporting standards. The paper concludes by discussing issues that could potentially arise if the standards are adopted in their entirety by the United States and the political issues that could emerge resultant of their adoption. The significance of international investment opportunities in foreign equity securities by investors in the United States and the significant number of foreign corporations registered on various securities exchanges around the world make the adoption and establishment of international reporting standards a challenge to many accounting professionals.

Keywords: International Financial Reporting Standards (IFRS); Multinational Accounting Practices; Global Accounting Standards

INTRODUCTION

Over the past several decades, progress has been made by many of the largest corporations as well as counties to harmonize financial accounting standards and practices into a single set of standards adopted by everyone. A single set of rules known as IFRS is currently being used by over 115 countries: including many in Africa, however the United States has yet to adopt IFRS standards (Doupnik & Perera, 2012). Some of the organizations who were instrumental in this project include the European Union (EU), the International Organization of Securities Commissions (IOSCO), and the International Accounting Standards Committee (IASC) (James, 2009). On November 14, 2008, the Securities and Exchange Commission (SEC) issued a proposal entitled, "Roadmap for the Potential Use of Financial Statements Prepared in Accordance with International Financial Reporting Standards by United States Issuers," which would force publicly traded companies in the United States to begin implementing the financial reporting standards set by IFRS after December 15, 2014. A corporation can request early adoption approval, if qualified, by the SEC for fiscal years ending December 15, 2009 (James, 2009). This major reporting change, if adopted by the United States, will affect accounting professionals who write standards, Accounting professors, Certified Public Accounting (CPA) firms, multi-national corporations, as well as businesses in the United States who are thinking about conducting business globally that have yet to start detailed training programs to assist in the understanding and implementation of IFRS. The current and growing breadth of the IFRS adoption suggests that IFRS has become a practical approach to achieving a single set of high quality, generally accepted standards for financial reporting worldwide.

LITERATURE REVIEW

As a single set of standards is introduced worldwide and the development of free trade and the interdependence of national economies continue to expand, it becomes necessary to perform due-process and to deliberate the potential advantages and disadvantages of having a single set of generally accepted standards to be used worldwide. According to Doupnik and Perera (2012), multinational corporations benefit from one set of standards due to the following reasons: a reduction in costs of the preparation of consolidated financial statements with the use of one set of standards, the reduction of costs of applying for an increase in capital assets in international markets and one set of standards assists with the analytics and comparability of financial statements from multiple locations of operation. Large multinational corporations also stand to realize the benefits with future mergers and acquisitions by having less onerous regulatory requirements, standardization of financial documents, capital allocation and more streamlined reporting when making financial decisions.

The greatest disadvantage of having a single set of standards include: the added costs of training professionals, the use the new standards and phasing out archived financial information previously reported under the old system into a newly adopted set of standards. There are other issues caused by instituting a single set of financial reporting standards worldwide. According to Doupnik and Perera (2012), the diversity of international accounting creates an extensively more complex arena for international corporations when preparing consolidated financial statements from the parent corporation's in compliant with US Generally Accepted Accounting Principles (GAAP)rules and regulations. One rationale is that this diversity presents a problem if international subsidiaries are responsible for recording transactions in two different sets of books. One of the financial records has to be recorded in the company's local GAAP rules and regulations and the other set of financial records has to be prepared according to the parent corporations standards. Diversity in accounting also creates issues with international companies trying to obtain permission to conduct business in foreign markets as many creditors and stakeholders want to have financial statements prepared in accordance with their local reporting standards. Accountants must measure performance accurately and fairly on a timely basis, so that corporations can attract investment capital and labor intensive dual financial records may slow the process and create inefficiencies (Doupnik & Perera, 2012). Finally, international companies may experience issues caused by diverse worldwide accounting standards when comparing financial statements and making foreign acquisitions.

Multinational corporations are interested in the potential benefits that could be derived from an international convergence of accounting standards. According to Doupnik and Perera (2012), the biggest advantage that results from the harmonization of financial reporting standards is the comparability at an international level. Some of the derived benefits could include: a decrease in costs of financial reporting for international companies that may place stock in international stock exchanges, a decrease in costs of consolidated financial statement preparation, and the negation of training when transferring accounting professionals to other subsidiaries.

A study conducted by Tyson (2011), analyzed several comment letters to the SEC on the final decision regarding the convergence (International Financial Reporting Standards, 2008). Many different viewpoints were discussed in these comment letters that were submitted to the SEC from interested parties, such as: Congress, international organizations, major firms, industries, multinational corporations, institutional investors, trade associations, accounting organizations, and academia. According to Tyson's study, a large part of responders, discussed the advantages of having a single set of financial reporting standards worldwide. The advantages mentioned in the comment letters included: " increased competitiveness of United States issuers in capital markets; a lower cost of capital for preparers and investors; process and cost efficiencies for multinational United States issuers and auditors; and an improved ability for investors to assess investment options" (Tyson, p. 26). Respondents also commented that the implementation of IFRS acknowledges principles-based IFRS standards, as opposed to the more rules-based United States GAAP which were designed to incorporate professional judgment and overall resulted in better clarity and transparency (Tyson, 2011).

Those respondents in disfavor of IFRS argued that the advantages of a one single set of international standards outweighed the costs of the implementation and transition of the standards (Tyson, 2011). Tyson stated, "Those arguing against conversion or adoption of IFRS identified a large number of disadvantages. These included: loss of control in the United States over standard setting; and large transition costs to implement IFRS, including employee training and IT systems occurring during a period of severe budget shortfalls and economic crisis" (p. 26). Other potential concerns according to Tyson involved the lack of evidence supporting the agreement that the IFRS were superior to the Generally Accepted Accounting Principles adopted in the United States and the omission of clarity on the FASB roles and SEC roles after the convergence of GAAP. An additional concern was the removal of an inventory method widely used in the US called Last-in-First-out (LIFO) under the IFRS and confusion surrounding several industry-specific rules under the IFRS. LIFO is an inventory valuation method used in accounting to value the cost of goods sold on the balance sheet found on a company's annual report. We do not know yet how comparability to prior financial data will be impacted by these changes dictated by the IFRS.

Lasmin (2011) conducted a study regarding the effects of the IFRS and convergence of GAAP on selected developing countries and determined that the International Accounting Standards Board (IASB) needed to ensure convergence among IFRS and national accounting standards was being met. Lasmin used the country of Indonesia as the basis of his study. According to Lasmin, the results of his study indicate that the third objective of the International Accounting Standards Board (IASB), promoting convergence between national accounting standards and IFRS, has been accomplished in Indonesia. The study also confirms that the efforts of Indonesian standards to increase the extent of harmonization of Pernyataan Standar Akuntansi Keuanga (PSAK) with IFRS have been successful. However, although the degree of material harmonization is relatively high, it is found that the improvement in formal harmonization is not followed by the progress of material agreement (p. 69-75).

INTRODUCTION OF THE PROBLEM

The on-going process and studies being conducted in the area of International Accounting will continue until a conclusion is reached on the convergence of most countries including the United States. The FASB has stated: "Investors would be better served if all United States publically held companies used accounting standards promulgated by a single global standard setter as the basis for preparing their financial reports. This would be best accomplished by moving United States public companies to an improved version of International Financial Reporting Standards (IFRS)" (Doupnik and Perera, 2012, p. 103). The move to IFRS in the United States will be extremely complex and will take several years to fully implement (Doupnik & Perera). Changes must be made to the United States financial reporting system, auditing standards, licensing requirements, and the education and certification of Accountants. The Security and Exchange Commission (SEC) was tasked to make a decision in 2011 on incorporating the IFRS in the United States, as of today no decision has been made by the SEC regarding this issue. The IASB must also remain attentive to the possibility that the decision could be unduly influenced by interested parties (Doupnik & Perera). Political pressures from various lobbying groups will be triggered upon the convergence of these standards due to some accounting treatments resulting in a more favorable outcome to some groups under IFRS (Doupnik & Perera). This impending controversy is highly probable at the onset of IFRS implementation (Tyson, 2011).

SIGNIFICANCE OF THE CONVERGENCE

Several important United States financial organizations are involved in the adoption of IFRS, including the FASB, who currently writes GAAP and the SEC and each of these organizations have different interests and end results in the final outcome of the convergence of GAAP into IFRS. Most of the companies that will be involved in the convergence are large multi-national companies, which, by default, will likely be publically traded companies governed by the SEC. Another issue that must be addressed is that if the FASB does adopt IFRS, but the SEC decides not to adopt IFRS how will this affect the overall adoption process since most of the companies that will be affected by the adoption are governed by SEC regulations. In addition, each international subsidiary would need to be responsible for recording transactions in two diverse sets of accounting books. One set of accounting books with the financial records recorded in the company's local GAAP rules and regulations and the other set of financial records would need to be prepared according to the parent corporation's standards. The international businesses that require financial statements for future acquisitions that are prepared according to the GAAP with which the parent company's managers have familiarity with will need a similar basis for comparison for properly analyzing and evaluating the business's overall financial position and operating results.

CONCLUSION

The issue of accounting standards convergence versus financial statement comparability should not be overlooked (Doupnik & Perera, 2012). Convergence of standards does not produce comparable financial statements. Although Accounting is the universal language of business, consistency in application and interpretation is likely to become a concern. Harmonization of common disclosures, common high quality auditing standards and practices and education and training of professionals is the goal of the convergence. Significant changes in the financial reporting environment are taking place and further research will need to be completed if a single widely accepted set of high quality accounting standards are to be adopted and a common platform on which corporations can report and investors can compare financial information.

AUTHOR INFORMATION

Ashley Harper is an adjunct instructor in the School of Business and Management. She was formally the Associate Department Chair of the Accounting Program at Kaplan University. She has been involved in teaching both traditionally and online since 2002 and has developed and taught accounting courses in all areas of accounting at both the undergraduate and graduate levels. Ashley's credentials are a MS from Louisiana State University with an emphasis in taxation and she is also licensed Certified Public Accountant (CPA) in the state of Louisiana, which is currently active. Ashley has just completed her accounting coursework towards her PhD in Accounting from Northcentral University and is currently working on her research courses towards her dissertation. Email: aharper@kaplan.edu (Corresponding author)

Linda Leatherbury is a full time faculty professor in the School of Business and Management where she teaches accounting and taxation courses. Dr. Leatherbury has been teaching for more than 15 years. Dr. Leatherbury obtained her Bachelor of Science Degree from Drexel University and her Masters of Taxation from Widener University. Her earned Doctorate of Philosophy (PhD) in Accounting is from Union University. Dr. Leatherbury worked 15 years at a major investment firm before beginning her teaching career. She has taught both face-to-face and online classes.

Ana Machuca is a full time professor in the School of Business and Management. She has been teaching since 1997 online and face-to-face and has been involved in administration, curriculum, and development within Kaplan University. Dr. Machuca's credentials are a Bachelor's Degree in Accounting and Finance from Florida Southern College, a Masters of Accounting and Financial Management (MAFM) from Keller Graduate School, a Master's in Business Administration (MBA) with concentration in Management from Webster University and a Doctor of Philosophy (PhD) degree in Business Administration with a specialization in Financial Management from Northcentral University. She is a Certified Public Accountant (CPA) and a Certified Fraud Examiner (CFE), which she uses for clients who hire her to investigate fraud.

JoDee Phillips is an adjunct instructor in the School of Business and Management. She was formally the Assistant Dean of Curriculum and Academic Department Chair with Kaplan University. She has been involved teaching online and assessing and creating curriculum for five years. JoDee's credentials are an MBA from Marylhurst University and she has passed her dissertation written comprehensive exam from Northcentral University working toward a PhD in Business with an emphasis in Marketing.

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