Global Convergence of Accounting Standards: The Role of FASB and IASB

Prof. (Dr.) T. Kama Raju

Professor, Dept. of Commerce and Management Studies,
Director - IQAC, Dr.B.R.Ambedkar University, Srikakulam, Andhra Pradesh

Abstract: The term 'Accounting Standards be defined as written statements issued from time to time by institutions of the accounting profession or institutions in which it has sufficient involvement and which are established expressly for this purpose. Such accounting institutions or bodies are currently found in many countries of the world, e.g. Accounting Standards Board (India). Financial Accounting Standards Board (USA), Accounting Standards Committee (Canada) etc. At the international level, International Accounting Standards Committee (IASC) has been created 'to formulate and publish, in the public interest, basic standards to be observed in the presentation of audited accounts and financial statements and promote their worldwide acceptance and observance.".

Keywords*:* Information Technology, Capital Markets, GAS, IFRS, Accounting Practice.

Introduction

With the advent of globalization in 1980's, compounded with the advancements made in information technology, the bottlenecks to free trade and movement of goods and services among global nations have been removed and economic interdependence among nations have been increased. Further, such transnational business operations have resulted into a phenomenal increase in cross-border securities trading and have heightened the significance of meaningful and comparable financial information. In general, the developed countries offer more organized, better-regulated and stable capital markets. Of them, the U.S. capital markets have long enjoyed the distinctions of being the market of first choice for non U.S. companies desiring to raise new capital or seeking to list their shares abroad.

Till recently, many countries had accepted the philosophy of harmonization of accounting standards. The logic was that different nations could have different standards as long as the financial statements prepared under the standards of one country could be adapted to the standards of another country and the differences could be reconciled. But with the growth in size and complexities of business, the differences in national accounting standards have mushroomed and this heightened the need to develop simply global accounting standards (GAS). One distinct advantage of having a set of high quality comprehensive GAS is that it cuts the cost of maintaining multiple sets of account books and preparing reconciliation statements.

Everybody realized that the cost of developing accounting standards collectively would be lower and the standards with a wider acceptance would be easier to enforce. There would be lower and the standards with a wider acceptance would be easier to enforce. There would be economies of scale and the developing nations with little or no experience in formulating accounting standards would also be able to participate in the process.

ISSN 2321-2926

The development of accounting standards is one of the landmarks in the history of evolution of corporate financial accounting and reporting. Accounting standards are the authoritative statements pronounced by professional accounting bodies that set the norms, rules and principles of measuring and reporting the transactions of the business. Accounting standards are now being formulated in a large number of countries although the institutional arrangements for setting such standards are different in different countries. At the country level, however, the US standard setting process is considered to be the best for its openness and rigor and also for issuing more than 141 standards on important and controversial areas.

Global Accounting Convergence

Convergence is a continuous process of ensuring that the Generally Accepted Accounting Principles (GAAP) are formulated, aligned and updated to international best practices (GAAPs in other countries) with suitable modifications and fine tuning considering the domestic conditions or trying to achieve at an international level consistency between its standards (IFRS) and those of national standards setters by drawing all parties to a single high quality solution – a process described as "Convergence".

The International Accounting Standards Board (IASB) has made a positive decision to seek convergence with national standard setters around the world. These intentions have been evident in actions such as the 'Norwalk Agreement' reached with the U.S. Financial Accounting Standards Board in October 2002, continuous discussions with representatives of accounting organizations and government bodies in the European Union, announcements of planned joint efforts with the Japan national standards setting body in 2004, as well as ongoing liaison activities with national standards setters that have taken place since the Board's inception. The Technical Committee is confident that the IASB is determined to solve the remaining issues causing differences in accounting among national standards setters and to create a high quality set of global accounting standards.

Need for Convergence

With the growing internationalization of trade and the globalization of business and capital market, financial information prepared according to the national accounting system of one country no longer satisfies the needs of users of other countries, whose decisions are more and more Global in scope. The pressure to adapt to the new Global environment therefore comes not only from the users of the financial information, but also from those who regulate and prepare them, that is the multinational corporations, the accounting profession and the Government and Revenue Authorities.

Benefits and Challenges of Convergence

Recognizing the fact that global capital markets require high quality, globally consistent and uniform regularity and accounting standards regime, most major capital markets are actively supporting the efforts of convergence towards a single set of globally accepted accounting standards. The role of International Organizations of Securities Commissions (IOSCO) has been examined. The benefits of globally accepted standards flow in the form of cost efficiencies to business and greater safe-guards to users. Put more specifically the benefits that would flow include the following:

§ It improves the comparability of investors to compare investment s on a global basis and thus lowers their risk of errors of judgment.

- For companies with global operations, it facilitates accounting and reporting and thus eliminates that cost involved in preparing multiple reports to meet regulatory requirements of different countries.
- Lowers the cost of the capital. The adoptions of the global standards such as IFRS may reduce the risk premium and, consequently, the cost of capital.
- More efficient allocations of resources, as it would eliminate barriers to cross – border listings.
- Higher economic growth.

Challenges:

- Environmental issues.
- Enforcement issues.
- Technical issues.

Organizations involved in Convergence

The organization involved in convergence may be put into two categories:

1. Those backed by international or political agreements
2. Voluntary organizations.

The first categories includes: the United Nations and the European Union. The second category includes: the international accounting standards board, the international Federation of Accountants, and the International Organization for Securities Commission, the European Financial Reporting Advisory Group, the Federation des Experts Compatibles, Europeans. There are many more bodies such as the Confederation of Asia pacific Accountants American Accounting Association, the British Accounting Association, the Indian Accounting Association, etc, That contribute to the convergence of accounting practice through conferences, researches, etc,.

International standards of accounting and reporting:

ISAR is the intergovernmental working group devoted to corporate transparency and accounting issues at the corporate level. It addresses a variety of issues in corporate accounting and reporting with a view to improving the global comparability and reliability of corporate reports. Its mandate is to:

- Make a positive contribution to standard selling at the national and regional levels.
- Take appropriate action to ensure the comparability of disclosures by TNCs.
- Review development in the field of international accounting and reporting, including the work of standard-setting bodies.
- Establish work priorities, taking into account the needs of home and host countries, particularly developing countries.
- Consult international bodies that it deems appropriate on matters pertaining to the development of international standards of accounting and reporting, and elicit the views of interested parties.
- Promote increased transparence and financial disclosure by encouraging the use of internationally recognized accounting and auditing standards and improved corporate governance.
- Report to the commission on Transnational Corporation (now the commission on Investment, Technology and Related Financial Issues) on steps to take, in pursuit of the long-term objective of international harmonization of accounting and reporting.

- Serve as an international body for the consideration of accounting and reporting falling within the scope of the commissions of the commission's work in order to improve the availability and comparability of information disclosed by transnational corporations.

ISAR accomplishes its mandate through an integrated programmed of research intergovernmental dialogue, consensus building and technical cooperation. In the context of convergence ISAR has undertaken country studies of Germany, Brazil, Kenya, India and Jamaica to examine the problems faced by these countries in implementing IFRS.

Benefits of Accounting Standards

The benefits of accounting standards may be listed as follows:

1. **To Improve the Credibility and Reliability of Financial Statements:-** Financial statements of business enterprises are used by a diverse group of users for making sound economic decisions. The users are shareholders (existing and potential) suppliers (existing and potential), trade creditors, customers, employees, taxation authorities and other interested parties. It is necessary, therefore, that the financial statements the users use and upon which they rely, present a fair picture of the position and progress of the enterprise. It is the function of accounting (and auditing) standards to create this general sense of confidence by providing a structural framework within which credible financial statements can be produced.
2. **Benefits to Accounting and Auditors:-** Accounting and auditors, with the passage of time and a changing climate of option, have to work in an environment where they face the threat of stem sanctions and bad name to their professions. These results partly from changed penalties and remedies available under the company law and partly from the greater willingness, the greater willingness of aggrieved parties to take their causes before the courts. Given the increasing risks, the accounting profession realized that it needed to know the accounting standards that are to prevail.
3. **Determining Managerial Accountability:-** Accounting standards facilitate in determining specific corporate accountability and regulation of the company. They help in assessing managerial skill in maintaining and improving the profitability of the company, depicting the progress of the company, its solvency and liquidity. Generally they are important factors in assessing the effectiveness of management's performance of its duties and leadership.
4. **Reform in Accounting Theory and Practice:-** Financial accounting has lacked, especially in the past, a coherent logical conceptual framework and structure for accounting measurements, financial reporting objectives and substantiated on accounting practice and usefulness of accounting data. This encouraged the emerging intelligentsia of accounting to develop accounting standards to improve existing practices or to rectify their defects.

ISSN 2321-2926

About the International Accounting Standards Board (IASB)

The International Accounting Standards Board, based in London, began operations in 2001 taking over from the former part-time IASC founded in 1973. It is funded by contributions from the major accounting firms, private financial institutions and industrial companies throughout the world, central and development banks and other international and professional organizations. The 14 Board members (12 of whom are full-time) reside in nine countries and have a variety of functional background. The IASB is committed to developing, in the public interest, a single set of high-quality; global accounting standards that require transparent and comparable information in general purpose financial statements. In pursuit of this objective, the ISAB cooperates with national accounting standard setters to achieve convergence in accounting standards around the world.

About the Financial Accounting Standards Board (FASB)

Since 1973, the Financial Accounting Standards Board has been the designated organization in the private sector for establishing standards of financial accounting and reporting in the United States. Those standards govern the preparation of financial reports and are officially recognized as authoritative by the Securities and Exchange Commission and the American Institute of Certified Public Accountants. Such standards are essential to the efficient functioning of the economy because investors, creditors, auditors and others rely on credible, transparent and comparable financial information.

The Norwalk Agreement:

In October, 2002, following a joint meeting at the offices of the FASB in Norwalk, Connecticut, the IASB and the FASB formalized their commitment to the convergence of generally accepted accounting principles in the US (US GAAP) and international Financial Reporting Standards (IFRSs) by issuing a memorandum of understanding. According to the MOU the two Boards pledged to put their best efforts to:

- ü Make their existing financial reporting standards fully compatible as soon as practicable and
- ü Co-ordinate their future work Programmes to ensure that once achieved, compatibility is maintained.

"Compatible" means that the two sets of standards do not conflict. Compatible does not, however, mean word-for-word identical standards.

The IASB – FASB Convergence Process

Various joint initiatives of IASB and FASB to achieve the goal of convergence include:

- Twice-yearly joint board meetings
- Aligned agendas, including explicit consideration of convergence potential in all agenda decisions
- Joint staffing of major projects
- Short-term projects to revise their individual standards to eliminate as many inconsistencies as possible
- A convergence research project seeking to identify all of the substantive differences between US GAAP and IFRSs and to develop strategies for resolving them. Any recognition, measurement, presentation or disclosure topic in which a specific

accounting treatment would be permissible under one basis of accounting but would not be permissible under the other basis of accounting is included in the project scope and

- Coordination between their respective interpretive bodies (FASB's Emerging Issues Task Force and the IASB's International Financial Reporting Interpretations Committee).

Between December 2003 and March 2004, the IASB amended the majority of the standards that it inherited from its predecessor, and it also issued several new standards. Many of those changes were in the interest of convergence. The current international standard on business combinations and goodwill (IFRS 3), for instance, is virtually identical to the FASB's recent standards.

FASB have completed the following short-term convergence projects:

- Financial Accounting Standards (FAS) 154, Accounting Changes and Error Corrections.
- FAS 153, Exchanges of Productive Assets.
- FAS 151, Inventory.

Specific short-term convergence projects currently under way include the following:

- By the IASB – provisions, segment reporting, government grants.
- By the FASB – earnings per share, fair value option for financial instruments, and research and development.
- Both boards – income taxes.

Similarly, many joint major projects have also been going on. They include the following:

- Business Combinations Phase II
- Revenue Recognition
- Performance Reporting
- Conceptual Frame work

On 11 September 2008, the IASB and FASB issued an update to report the progress they have made since 2006 and to set the global for completing the major projects by 2011. The projects relating to financial statement presentation, leases, liabilities and equity distinctions, revenue recognitions and post–employment benefits (including pensions) are expected to be completed by 2011. In case of fair value measurement the FASB has already issued a standard in 2006; in case of IASB the project is expected to be completed by 2010. For the consolidations' project both boards are expected to issue final standards by 2009-10. In case of de-recognition also both boards are likely to issue final standards in 2009-10. The business combinations project was already completed in 2007, both boards issued revised standards.

There exist a lot of differences between the standards issued by the FASB and those issued by the IASB or its Predecessor body, viz., IASC. A comparison among these standards will pinpoint these differences. A realistic short-term goal of convergence is to reduce the number of differences between the two sets of standards so as to cause the least amount of disturbance to the capital markets. The IASB has also taken initiative with the objective of attaining convergence of the IFRS with the accounting standards of seven other countries (e.g. Australia and New Zealand, Canada, France, Germany, Japan and the United Kingdom). All these steps are intended to lead to emergence of "global accounting standards". So far as India is concerned, the position is not different. If one compares the standards issued by the ICAI with those issued by the IASC/IASB, then many differences are noticed. So, India will also greatly benefit from the convergence proves because Indian accounting standards are based on the IASB standards.

Conclusion:

Accounting standards setting is a continuous process that must respond to changes and developments in the markets and the information needs of investors. Accounting information should be reliable in use so that users of accounting information may be able to rely one some basic assumptions about the quality of accounting information produced by accountants. But in practice the accounting profession has failed to give reliable information to investors about the true state of affairs of a number of celebrated companies. Consequently, the need for international accounting standards has become imperative.

References

Accounting Principles Board. (1972), "Accounting for Stock Issued to Employees." Opinions of the Accounting Principles Board No. 25, New York: AICPA, 1972.

Casabona, P. and V. Shoaf. (2002), "International Financial Reporting Standards: Significance, Acceptance, and New Developments," Review of Business, 23(1), pp. 16-20.

Financial Accounting Standards Board, FASB-IASB joint meeting supports convergence, The FASB Report, Norwalk, CT: FASB, September 30, 2002.

Financial Accounting Standards Board, International accounting standard setting: a vision for the future, Norwalk, CT: FASB, 1998.

International Accounting Standards Board, IASB Insight; The newsletter of the International Accounting Standards Board, London: IASB, January, 2003.

International Organization of Securities Commissions. (2000), "IASC Standards," Report of the Technical Committee of the International Organization of Securities Commissions (with Appendixes), May 2000.

Lipe, R. (2001), "Lease Accounting Research and the G4+1 Proposal," Accounting Horizons, 15(3), pp. 299-310.

Pownall, G. and K. Schipper. (1999), "Implications of Accounting for the SEC's Consideration of International Accounting Standards for U.S. Securities Offerings," Accounting Horizons, 13(3), pp. 259-280.

Shriram Rathore, (2009), International Accounting, PHI Learning Private Ltd., New Delhi.

Tidrick, D.E. (2002), "A Conversation with James J. Leisering, IASB Member," The CPA Journal, 72(3), pp. 48-51.

Tweedie, D., Sir. (2001), "IASB Chairman's Report: Support for a New International Standard-Setter," IASCF Annual Report 2001, pp. 4-10.

Website at www.dca.com accessed on 20th April 2013.

Website at www.fasb.org/intl. accessed on 5th august 2013.

Website at www.iasb.org.uk accessed on 8th august 2013.