

Ross Roundtable
On
International Accounting Standards: Where is the U.S.A.?

The terms harmonization and convergence have both been used to describe efforts by the United States and European countries to move towards a global financial accounting infrastructure. Is there a fundamental difference between harmonization and convergence? At what point did the efforts that started as harmonization become convergence? The participants at the Ross Roundtable of the NYU Stern School of Business clearly were not in harmony on the prospects of the convergence of US GAAP to IFRS.

Definition will play an important role in efforts toward creating global accounting standards. Harmony does not adopt a one-size-fits-all approach, but accommodates national differences. Very few of us would argue with expending efforts towards this end. Convergence on the other hand is *moving together toward a common result*. The FASB and the SEC have changed the agenda from harmonization to convergence. It became evident during the Roundtable discussions that participants were *not in sync*. The convergence towards global accounting standards is being met with mixed emotions.

Just how much pressure is on the FASB to converge? We have witnessed the fallout of home-grown political pressures. The results are inconsistent standards, e.g. pension accounting, ESO's, etc.. If we add global political pressures to the mix, what can we expect in terms of accounting standards that will embody the qualitative characteristics set forth in the FASB Conceptual Framework? The U. S. has been a magnet for capital from every corner of the globe. Clearly one of the reasons has been transparency, full disclosure, and above all oversight and regulation of our markets. Why open the floodgates? There was a consensus of opinion among the participants that even if convergence to consistent, quality global accounting standards were achieved, problems of interpretation, implementation, and regulation (enforcement) would still persist. What progress has been made towards resolving these issues?

The U. S. and European interpretative bodies, the EITF and the IFRIC, are working together in an effort to eliminate differences in interpretation of similar standards. The SEC and the International Organization of Securities Commissions [IOSCO] signed a Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information [MOU]. All EU-listed public companies will be required by the European Union to prepare their consolidated financial statements using IASB Standards.

In October 2002, the FASB and the International Accounting Standards Board (IASB) announced the issuance of a memorandum of understanding ("Norwalk Agreement"), marking a significant step toward formalizing their commitment to the convergence of U.S. and international accounting standards. Joint projects being conducted currently relate to revenue recognition and business combinations. These projects fall under the "short-term convergence projects", where convergence consists of selecting between existing U. S. GAAP and IFRS. The participants were skeptical as to the outcome of this "cherry picking" endeavor. Furthermore, topics that will increase convergence will receive priority placement on the Board's agenda. Where does that leave the average U.S. investor?

The SEC is preparing for a time when IFRS financial statements can be accepted without reconciliation. They believe that having one set of high quality standards would reduce the cost of capital around the world. Towards this end, IFRS and FASB projects are treated in similar fashion. The SEC is also working with IOSCO, IFAC, and the IASB on all aspects of international convergence. Participating scholars commented that there was no theoretical or empirical evidence for assuming that the cost of capital was solely related to financial disclosures; perhaps costs are also being driven by trading systems

The SEC concurs with the FASB's decision to place issues on the agenda that facilitate convergence rather than having priority in their own right. The participants of the Roundtable question the legitimacy of these efforts, and whether there has been full disclosure of the FASB's revision of their agenda-setting process. Basic to the convergence debate has been the "principles-based versus rule-based standards argument. The SEC has added a new term to the mix; "objective-oriented" standards. It is important to remember that the detailed guidance that exists in U. S. GAAP today evolved in efforts to avoid litigation. This is a problem that has yet to emerge in other markets.

A European SEC? The European Commission (EC) has established two committees. The European Securities Commission (ESC) and the Committee of European Security Regulators (CESR). The committees will act as regulatory committees, develop basic legislation, and develop and promote consistent implementation measures between national regulators. The CESR has issued for comment a Draft Statement "Principles of Enforcement".

Undoubtedly, the foundation for building a global financial accounting infrastructure is in place. The major players are pursuing convergence. The participants of the Roundtable all agreed that transcending cultural, environmental, and political differences in the objectives of financial reporting may not be fully achievable. The SEC has commented to the effect that "multiple interpretations that make sense will be acceptable". Because of different environmental and cultural influences, differences in accounting may be appropriate. There was a consensus of opinion that the objective of "decision useful information" transcends national borders. However, although the Conceptual Framework states "useful to...investors and creditors", in the U. S. it is the investor that is key. In other countries creditors (banks), taxing authorities, and government agencies are the key players. The objectives, qualitative characteristics, and principles outlined in the FASB Conceptual Framework provide a strong foundation for promulgating global accounting standards. Dealing with problems in the definition of the elements of financial reports, and interpretation thereof, will remain obstacles to achieving convergence.

Harmonization has morphed into convergence. International efforts and resources are being expended towards this end. The FASB is placing domestic issues on the "back burner", and the SEC is actively pursuing liaisons with the International Community. Increasing market efficiency and reducing the cost of capital are given as the primary reasons. There is, however, inconclusive evidence that convergence of accounting standards will bring about the desired result. Just where does this leave the small U. S. investor? Why is the SEC and FASB pursuing

convergence, as opposed to harmonization, proactively? The reasons are less than transparent because harmonization may have a greater chance of success.