The importance of global standards

ACCA believes that global standards are important, not only for the accountancy profession, but for the world economy. 2011 is a big year in this respect and decisions made in the next few months could have major implications for many years to come.

A sound financial reporting system, supported by high quality accounting and auditing standards and backed by a solid regulatory, governance and ethical framework, is a pre-requisite for economic development. Investors will not trust in financial information unless it has this underpinning and so economic activity and prosperity will not take place.

This can of course take place at national level, but the benefits increase if the standards are global. Investors and lenders will be much more willing to do business across borders if they are able to rely on financial information based on a set of standards familiar to them. This was the whole logic of the introduction of International Financial Reporting Standards (IFRS), on which ACCA has based its syllabus since 1996. The wider move to IFRS was given fuel-injection by the Asian financial crisis of 1997-8. This crash showed the weaknesses, in the eyes of Western investors, of a system where accounting standards and corporate governance systems were so different in an important economic region.

Research carried out by ACCA ten years after that crisis showed that CFOs in Malaysia, Singapore, Hong Kong and mainland China strongly supported the adoption of IFRS, believing it added value to the Asian capital markets by creating easy comparability for western investors and by allowing a principles-based approach. And a follow-up survey we carried out in late 2008 showed that 500 CFOs across Europe, Asia and the US agreed on the benefits of global reporting standards.

The advantages are worth repeating:
- they encourage transparency and easy comparison in transactions crossing borders and jurisdictions
- translation and reconciliation costs are removed
- all companies are better able to attract capital from a larger pool of investors, driving down costs of capital
- opportunities for regulatory arbitrage are eliminated

These benefits aid both businesses and regulators. Cross-border mergers and acquisitions activity and strategic investment are facilitated while national regulators (in the absence of global regulation) can work together and develop supervisory practices which are more closely aligned.

A separate study commissioned by ACCA at the same time also revealed that UK companies had seen a reduction in costs of capital of between 1-2% since the introduction of IFRS in 2005 while for the EU as a whole, the figure was 1%. It appears that in countries where equity-based financing dominates, and corporate disclosure quality is already high, the implementation of IFRS leads to greater rewards.
The ACCA CFO survey also showed CFOs believed the same logic applied outside financial reporting in areas such as sustainability reporting. Although they had less direct awareness of this area than the financials, those who had personal experience of regimes such as that of the Global Reporting Initiative agreed that such international frameworks delivered business benefits.

In the two years since those ACCA studies, the position of accounting has been elevated to centre stage on the agenda of world leaders, who have used the last three G20 summits to put their weight behind calls for one set of global financial reporting standards. The world financial crisis has upped the ante and accounting standards, like common capital requirements, are increasingly seen as crucial to prevent any repetition of the crisis in future.

They are also seen as helping to provide a bulwark against any retreat into protectionism by countries facing economic uncertainty. With the Doha round of the WTO still incomplete, an estimated $170bn could be lost or added to the global economy, depending on how those free trade talks progress in 2011. A weakening of the move to international accounting standards at this stage could be costly.

Already 122 countries use IFRS, with a similar number now adopting international standards on auditing (ISAs). The revised, so-called ‘clarity ISAs’ have proved successful and the EU is the most important remaining region where these are only permitted, rather than mandated, a position ACCA would like to see reversed.

On IFRS, 2011 will see the global spread of these standards approaching the final and highest fence. If the US agrees to adopt them, not only will that see the world’s largest capital market joining in, but it will also give a strong signal to those countries which have yet to decide on IFRS to follow their lead. Some countries are taking the view that only a yes from the US would see a genuinely global system. A ‘no’ would have serious consequences not only for US companies, who would face continuing costs in maintaining multiple sets of accounting books (reporting under US GAAP at home and IFRS in their overseas subsidiaries) but also further afield.

Of course the US authorities will only join if they think the standards themselves are of similar high quality to their own regime. Intense work is being carried out by the two standards setters, the IASB and US FASB, to iron out differences ahead of a final decision by the SEC later this year, although there is a limit to how far this ‘convergence’ can go given the predominantly principles-based nature of IFRS compared with a largely rules-based US tradition. The US will ultimately have to take, to some degree, a leap of faith although the changes would not come into effect until 2016.

This would not be a problem. Such a major change takes time in terms of preparation, training etc. What would be a problem would be a ‘no’ decision. Like the Doha round, worldwide support could easily slide away and the whole process unravel. Already the EC is giving less than helpful indications that its patience is running out and US prevarication could see moves to a European accounting system. After so much effort over the past 10 years since the IASB’s formation, such an outcome would be little short of a disaster both for the profession but more importantly for international business, just as would ultimate failure of the Doha talks this year. Global standards
and international free trade go together, and are essential as the world economy recovers from the recent crisis. Recent indications from Washington are promising and we must all hope they turn into a formal ‘yes’ later this year.

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