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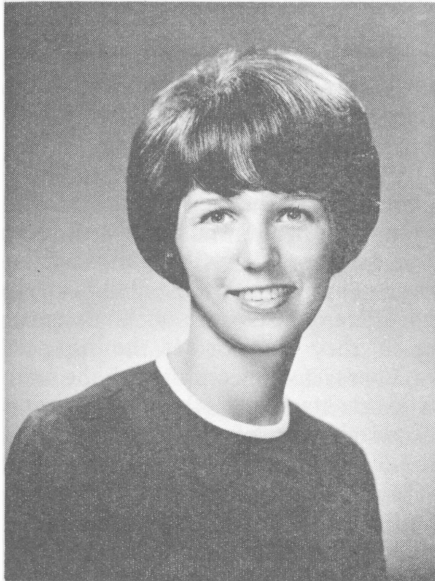
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# The Development of International Accounting Standards



Jan Giannini Brown

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*"International accounting...is not a separate subdiscipline of the subject (of accounting) but rather practiced by various nations in their efforts to control and direct the activities of their particular business communities. Achieving any measure of harmonization among these diverse accounting practices requires altering either the business practices or the political thrust of the national system. Accounting is accounting; its proper application is the crux of the international problem."<sup>1</sup>*

Legal framework and institutions, as well as local politics, have dominated the growth of the accounting profession in many countries. As a result there is wide variation in "generally accepted accounting principles." This paper examines the international accounting environment and the search for international accounting standards.

## The Problem

Accounting has developed at various rates throughout the world. It reflects not only differing stages of economic development but also many political influences, government regulations, and development or non-development of professional accounting organizations. According to Australia's Dr. Raymond Chambers, accounting is the same throughout the world; its function of communicating and analyzing financial data is universal.<sup>2</sup>

But there are problems in international accounting. They stem from the external political and legal constraints which distort the function of accounting to serve other interests. Efforts to harmonize accounting standards are hindered by these constraints. National professional organizations are also reluctant to give up sovereignty

over their jurisdictions.

There are those who believe the attempts to achieve a degree of uniformity in international accounting are unnecessary and/or impractical. Some contend that standards in the United States are superior to those of other countries, that attempts to achieve international standards conflict with the work of the Financial Accounting Standards Board, and that implementing international accounting standards may be impractical since the FASB has the dominant power of establishing U.S. accounting standards. Doubtless, similar arguments by other national interests have similar application in other countries.

Proponents of international accounting standards argue that international accounting standards will help investors in multinational corporations and help the multinationals to take advantage of foreign securities markets because financial statements will be more comparable. In an age when multinational investing is a daily occurrence the development of international accounting standards is essential and long overdue.

## Accounting in Various Countries

It is enlightening to look briefly at accounting as it exists in various countries.<sup>3</sup> At once the problem of international accounting becomes more than one of accounting for foreign currency translation, although that is undeniably a major concern.

### Germany

The approach in setting German accounting standards is strictly legalistic and standards are set by politicians. Tax regulation requires that tax deductions also be deductions in financial reports. Deferred charges are excluded from assets. Income or loss is the difference between net assets at the beginning and end of a period, adjusting for withdrawals and capital contributions. German accounting standards provide convenient opportunities for the management of income.

### Mexico

There is one national accounting association, the Mexican Institute of Public Accountants, which sets uniform professional guidelines. Although inflation has been rampant in the past few years, price-level accounting is accorded little or no consideration. Upward revaluation of fixed assets, however, is acceptable. Depreciation is taken on the increased amount of fixed assets.

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## The International Accounting Standards Committee...“a most promising development”

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Preparation of consolidated financial statements is rare.

### British Isles

As a result of some notorious instances of aberrations in accounting practices from company to company, the Accounting Standards Steering Committee (ASSC) was established in 1969 and has issued six Accounting Standards. This organization has been given the full support of the stock exchange council.

### Canada

The Canadian Institute of Chartered Accountants (CICA) Accounting and Auditing Research Committee and its successors have the right to publish “Recommendations” in the CICA Handbook. These Recommendations must be complied with and any departures must be disclosed and justified.

### France

There are many types of professional accountants, each with separate directives. Accounting is regulated more by law — commercial, tax, and other bodies — than by the profession. Most accounting principles are similar to those of the United States. However, financial statements issued to shareholders and those incorporated in tax reports must be in basic agreement. Bad debts must be identified before being written off. Income tax allocation is nonexistent. Footnotes are rare but are being encouraged.

### Egypt

Objectives of the Egyptian uniform system of accounting are to facilitate national planning and control, permit the screening of inefficient enterprises and provide information for management.<sup>4</sup>

These six glimpses, although brief, highlight some of the areas of national

differences, and underscore the observation in a summary discussion of Accounting Principles Board Statement No. 4, Chapter 9, as amended:...“prerequisite to the development of accounting standards on an international scale is...a knowledge of accounting practices and principles in various countries.”<sup>5</sup>

## Geographically Related Organizations

In recognition that alternatives in accounting practice must be narrowed, many regional accounting organizations have sprung up. The Inter-American Accounting Conference, the Conference of Asian and Pacific Accountants, and the Union of European Accountants share the objective of furthering understanding among professional accountants in different countries. In addition, the European Economic Community Accountants' Study Group prepares recommendations for harmonizing prevailing accounting practices. Generally, it has accepted the prevailing practices and recommended elaborate disclosures. A true and fair view of a company's financial position and results of operations is emphasized. The Accountants' International Study Group compares accounting and auditing standards in the United Kingdom, the United States, and Canada to promote greater international harmony. The International Committee for Accounting Cooperation assists in the improvement of accounting education and the practice of public accounting in developing countries.

## The IASC

The International Coordination Committee for the Accountancy Profession (ICCAP) was formed in 1972 at a meeting of the International Congress. Its purpose is to develop a coordinated worldwide accountancy profession with uniform professional standards. In 1973, the nine-nation International Accounting Standards Committee (IASC), of which the American Institute of Certified Public Accountants is a participant, was formed as an independent arm of the ICCAP. Its purpose is to formulate and publish basic standards to be observed in the presentation of audited accounts and financial statements and to promote their worldwide acceptance and observance.

There are two classes of membership in the IASC. Founding member coun-

tries, of which there are nine, have one vote. Exposure drafts require assenting votes of two-thirds of the founding members. Statements of International Accounting Standards require three-fourths assenting votes of the founding members. Associate memberships for institutes are also permitted. These institutes may then nominate individuals for specific assignments and service on working parties.

The IASC determines the topics for possible issuance of standards. As of July, 1977, the IASC has issued, or approved for issuance, seven statements in final form, exposure drafts of five others, a discussion paper on accounting for price changes, and has additional topics under study. (See appendix)

Members of the IASC have agreed to support the IASC standards and to do their best to ensure the published accounts comply with these standards, or that there is disclosure of the extent to which they do not. If the financial statements do not comply with the international standards the audit report should either refer to the disclosure of noncompliance in the financial statements, or state the extent to which the financial statements do not comply. Members have also agreed to assert their best efforts to take appropriate action against auditors who do not comply with IASC standards, and to persuade governments and other authorities as well as the business community that published financial statements should comply with the standards.

Because it is realized that no country would relinquish its sovereignty in setting accounting standards, local standards prevail, but noncompliance with international standards must be disclosed. It is hoped that disclosure of noncompliance will bring pressure on either local accounting organizations or the IASC to change the standard or set new standards.

Gerhard Mueller and Lauren Walker believe “the work of the IASC is without doubt the most promising development ever with respect to setting and achieving a measure of adoption for international accounting standards.”<sup>6</sup> So far the IASC Standards have involved areas of minor differences. As the IASC progresses into other areas, many controversies may arise. To meet its objectives, the IASC will need the support of all parties involved.

An International Federation of Accountants has been proposed to replace the ICCAP. Its purpose would be to develop and enhance a coordinated worldwide accounting profession with harmonized standards. It would encourage efforts to establish international technical, ethical and educational guidelines for the accounting profession. The IASC would continue as an independent body and work closely with the new federation. A formal recommendation to establish this body will be made at the International Congress at Munich in October 1977.

#### U.S. Support For The IASC

The United States has indicated its support of international accounting in general and international standards in particular. In October 1975 the FASB issued Standard No. 8 on Foreign Currency Translation. This Standard requires among other things that foreign exchange translation gains and losses be currently recognized in the income statement.

The AICPA has published a book that describes accounting practices in thirty countries. In addition, the AICPA supports a staff to deal with international accounting problems.

In July 1975 the Institute reaffirmed its support of the IASC and made the following points:

1. To be accepted, IASC Standards will have to be adopted by the FASB.
2. If there is no significant difference between international and U.S. Standards, compliance with U.S. GAAP constitutes compliance with the international standards. Areas of differences should be given early consideration by the FASB to harmonize the differences.
3. Published pronouncements by the IASC will be included in the appropriate volume of AICPA Professional Standards, indicating

any significant differences between international and U.S. GAAP.

4. The AICPA will encourage all pertinent parties to respond to IASC exposure drafts.<sup>7</sup>

#### Conclusion

Different cultures create different standards for comparing financial statements, different investment institutions have different needs, and accounting principles differ from country to country. To deal with these problems, there are three schools of thought: primary and secondary financial statements<sup>8</sup>, single domicile reports with limited restatement, and international reporting standards. This paper has dealt with the latter.

The problem is to convey the same message to a foreign user as that received by a native user. Some believe that the dual, primary and secondary system is the most practical approach until the international standards are firmly established.

Ideally, with identical reporting standards, transactions would be recorded the same the world-over. There are many differences to account for and in present accounting practice it often happens that the same event in two different countries will result in two different reports.

It seems appropriate to again quote from Irving L. Fantl who authored the opening quotation: "It were best to harken to the old cliché, to recognize the difference between that which we can improve and that which we cannot change and to change the one while we learn to live with the other."<sup>9</sup>

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*Editor's Note: Ms. Brown's article deals with financial accounting rather than management, government, or social accounting. It is therefore restricted to a discussion of the measurement and reporting of financial activity of the firm.*

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**"In an age when multinational investing is a daily occurrence the development of international accounting standards is essential, and long overdue."**

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#### FOOTNOTES

<sup>1</sup>Irving L. Fantl, "Frustrations Facing Accounting Uniformity," *The Accounting Forum*, (Vol. 46, No. 1, May, 1976), p. 28.

<sup>2</sup>*Ibid.*, p. 27.

<sup>3</sup>International Accounting Developments: A Symposium," *The Arthur Andersen Chronicle*, (Volume 34, Number 3, July, 1974), pp. 67-95.

<sup>4</sup>"Report of the American Accounting Association Committee on International Accounting, 1974-75," *The Accounting Review*, (Supplement to Volume XLXI, AAA, 1976), p. 73.

<sup>5</sup>*Professional Standards* Volume 3, Accounting As of Sept. 1, 1975, (Chicago, Illinois: Commerce Clearing House, 1975), paragraph 1029.12, p. 7334.

<sup>6</sup>Gerhard G. Mueller and Lauren M. Walker, "The Coming of Age of Transnational Financial Reporting," *The Journal of Accountancy*, (Volume 142, No. 1, July, 1976), p. 73.

<sup>7</sup>*Ibid.*, pp. 71-73.

<sup>8</sup>Gerhard G. Mueller, "The Dual System for Transnational Financial Reporting," *The Accounting Forum*, (Vol. 46, No. 1, May, 1976), p. 17.

<sup>9</sup>Fantl, op. cit., p. 29.

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**In Any Language, In Any Country, Business Needs ..... The Accountant**

## **APPENDIX**

### **INTERNATIONAL ACCOUNTING STANDARDS COMMITTEE PROGRESS AS OF JULY 1977**

#### **Standards Issued**

- IAS No. 1 Disclosure of Accounting Policies**
- IAS No. 2 Valuation and Presentation of Inventories in the Context of the Historical Cost System**
- IAS No. 3 Consolidated Financial Statements**
- IAS No. 4 Depreciation Accounting**
- IAS No. 5 Information to Be Disclosed in Financial Statements**
- IAS No. 6 Accounting Responses to Changing Prices**
- IAS No. 7 Statement of Changes in Financial Position**

#### **Exposure Drafts Issued**

- E 8 The Treatment in the Income Statement of Unusual Items and Changes in Accounting Estimates and Accounting Policies**
- E 9 Accounting for Research and Development Costs**
- E10 Contingencies and Events Occurring After The Balance Sheet Date**
- E11 Accounting for Foreign Transactions and Translations of Foreign Financial Statements**
- E12 Accounting for Construction Contracts**

#### **Topics Under Study**

- 1. Accounting for Taxes on Income**
- 2. Accounting for Diversified Operations**
- 3. Accounting for Leases in The Financial Statements of Lessors**
- 4. Working Capital**
- 5. Disclosure in Financial Statements of Banks**
- 6. Accounting for Pension Costs and Commitments**