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Whose Trojan Horse? The Dynamics of Resistance Against IFRS

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WHOSE TROJAN HORSE? THE DYNAMICS OF RESISTANCE AGAINST IFRS

MARTIN GELTER* & ZEHRA G. KAVAME EROGLU**

The introduction of International Financial Reporting Standards (“IFRS”) has been debated in the United States since at least the accounting scandals of the early 2000s. While publicly traded firms around the world are increasingly switching to IFRS, often because they are required to do so by law or by their stock exchange, the Securities Exchange Commission (“SEC”) seems to have become more reticent in recent years. Only foreign issuers have been permitted to use IFRS in the United States since 2007. By contrast, the EU has mandated the use of IFRS in the consolidated financial statements of publicly traded firms since 2005. In the United States, IFRS, which are promulgated by the London-based International Accounting Standards Board (“IASB”), are often seen as an attempt by Europeans to colonize U.S. accounting standard setting, and as an element of a foreign legal system alien to U.S. capital markets and securities law. In this article, we suggest that this perception is actually a myth, which we attempt to debunk. In fact, the introduction of IFRS in Europe, particularly Continental Europe, was far from controversial. IFRS were promoted by Anglo-Saxon jurisdictions and strongly supported by the United States, particularly when capital markets internationalized in the 1990s. They were – and still are – in many ways at odds with the Continental European accounting cultures of countries such as France and Germany, on whose examples we draw. In spite of the EU mandate for publicly traded firms, accounting law in these jurisdictions

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has still not fully absorbed IFRS; nevertheless, for now a solution that reconciles traditional and international accounting has been found. In this article, we explore the problems and resistance of IFRS in Continental Europe and seek to draw lessons for the United States. We argue that given the shared heritage of U.S. Generally Accepted Accounting Principles ("GAAP") and IFRS as investor-oriented accounting standards, their introduction in the United States should be considerably easier than it was on the other side of the Atlantic.

*"IFRS are dangerous and obsolete."
(from a French accounting textbook published in 2011)¹*

¹ JACQUES RICHARD, CHRISTINE COLLETTE, DIDIER BENSADON & NADINE JAUDET, *COMPTABILITE FINANCIERE: NORMES IFRS VERSUS NORMES FRANÇAISES 1* (9th ed. 2011).

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1. INTRODUCTION

The United States is the last major economy that has not yet adopted International Financial Reporting Standards (“IFRS”) while, from Europe to Canada, from Australia to China, around 120 countries are already requiring or permitting IFRS; this figure will likely rise to 150 countries in the near future.² The introduction of IFRS has been debated in the United States for several years.³ The Securities and Exchange Commission (“SEC”) first issued a paper that included a plan for possible implementation, and several SEC Staff Reports followed up until the July 2012 Final Staff Report with regard to the work plan.⁴ However, whether

² *Analysis of the IFRS Jurisdictional Profiles*, IFRS (last updated Sept. 25, 2014), <http://www.ifrs.org/Use-around-the-world/Documents/Jurisdiction-Profiles.pdf>, (listing and outlining profiles of countries adopting IFRS for publicly traded firms); Geoffrey Pickard, *Simplifying Global Accounting*, J. ACCT., July 2007, at 36 (providing an interview with Sir Tweedie discussing “the future of IFRS, U.S. GAAP and the global accounting profession” and reporting Tweedie’s prediction that the number of countries requiring or permitting IFRS will rise to 150); see Sir David Tweedie, Chairman of the International Accounting Standards Board, Speech at Empire Club of Canada at the Toronto Conference (Apr. 25, 2008) (discussing the existence of a “clear momentum towards accepting IFRS as a common financial reporting language throughout the world.”); Lawrence A. Cunningham, *The SEC’s Global Accounting Vision: A Realistic Appraisal of a Quixotic Quest*, 87 N.C. L. REV. 1 (2008) (critiquing the SEC’s approach, as set out in the SEC Concept Release of Aug. 7, 2007, *infra* note 4).

³ See generally Peter White, *It’s Greek to Me: The Case for Creating an International Agency to Enforce International Accounting Standards to Promote Harmonization and International Business Transactions*, 27 WIS. INT’L L.J. 195 (2009).

⁴ Concept Release on Allowing U.S. Issuers to Prepare Financial Statements in Accordance with International Financial Reporting Standards, Exchange Act Release Nos. 33-8831, 34-56217, Fed. Sec. L. Rep. (CCH) (Aug. 7, 2007) [hereinafter SEC Concept Release] (requesting information about whether U.S. issuers should be permitted to prepare financial statements in accordance with IFRS to satisfy SEC rules and regulations); see Roadmap for the Potential Use of Financial Statements Prepared in Accordance with International Financial Reporting Standards by U.S. Issuers, Exchange Act Release Nos. 33-8982, 34-58960, Fed. Sec. L. Rep. (CCH) (Nov. 14, 2008) [hereinafter SEC Roadmap, November 14, 2008] (proposing a roadmap to allow the use of IFRS by U.S. issuers for the purpose of the SEC filings); Office of the Chief Accountant, Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers: Final Staff Report (July 13, 2012) [hereinafter SEC Final Staff Paper, July 13, 2012], available at <http://www.sec.gov/spotlight/globalaccountingstandards/ifrs-work-plan-final-report.pdf> (summarizing results of key areas identified for study in the SEC Work Plan); Office of the Chief Accountant, Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers: A Comparison of U.S. GAAP and IFRS, A Securities and

domestic issuers should be permitted to use IFRS is very controversial. Obviously, the “internationalization” of accounting would have far-reaching consequences for U.S. firms, for the relationship between managers and investors, for the accounting profession, and for the position of the U.S. Financial Accounting Standards Board (“FASB”) within the framework of securities law.

The European Commission’s decision in 2000 to mandate the use of IFRS starting from 2005⁵ and the unprecedented worldwide

Exchange Commission Staff Paper (Nov. 16, 2011) [hereinafter SEC Staff Paper, Nov. 16, 2011] (summarizing results of SEC evaluation of areas in which IFRS provides less guidance than GAAP); Office of the Chief Accountant, Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers: Exploring a Possible Method of Incorporation, A Securities and Exchange Commission Staff Paper (May 26, 2011) [hereinafter SEC Staff Paper, May 26, 2011] (outlining a possible approach for incorporating IFRS in the U.S.); Office of the Chief Accountant, Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers, Progress Report (Oct. 29, 2010) (outlining progress made on achieving objectives outlined in the SEC Work Plan, *infra*); Office of the Chief Accountant, Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting System for U.S. Issuers, Appendix to SEC Release No. 33-9109 (Feb. 24, 2010) [hereinafter SEC Work Plan], available at <http://www.sec.gov/rules/other/2010/33-9109.pdf> (considering specific issues relevant to whether the SEC transition U.S. issuers to a system incorporating IFRS); IFRS Foundation, Report to the Trustees of the IFRS Foundation, *IFRS Foundation Staff Analysis of the SEC Final Staff Report – Work Plan for the Consideration of Incorporating IFRS Into the Financial Reporting System for US Issuers* (Oct. 22, 2012) [hereinafter October 2012 IFRS Foundation Report].

⁵ To be precise, the requirement only applies to the consolidated financial statements of all those companies governed by the law of a Member State and listed on a regulated market in a Member State. See Regulation 1606/2002, 2002 O.J. (L 243) 1 (EC) [hereinafter IAS Regulation] (“The Lisbon European Council of 23 and 24 March 2000 . . . set the deadline of 2005 to implement the Commission’s Financial Services Action Plan and urged that steps be taken to enhance the comparability of financial statements prepared by publicly traded companies.”); see also Institute of Chartered Accountants in England and Wales (ICAEW), *EU Implementation of IFRS and the Fair Value Directive: A Report for the European Commission* 19–24 (Oct. 2007), available at http://ec.europa.eu/internal_market/accounting/docs/studies/2007-eu_implementation_of_ifrs.pdf (reporting on the implementation of IFRS within the EU). The requirement applies to Member States of the European Economic Area (“EEA”), which consists of the twenty-seven EU member states plus Iceland, Liechtenstein, and Norway. Regarding the application of the Accounting Directives in the EEA, see Paul Pacter, *What Exactly is Convergence?*, 2 INT’L J. ACCT., AUDITING & PERFORMANCE EVALUATION 67, 75 (2005); Deloitte, *IFRS in Europe – Background Information*, IAS PLUS (last visited Sept. 26, 2014), <http://www.iasplus.com/en/resources/ifrs-in-europe> (containing information about the IFRS in Europe from 2001–2014); see also Robert K. Larson & Donna L. Street, *The Roadmap to Global Accounting Convergence: Europe Introduces ‘Speed*

acceptance of IFRS since then prompted a debate about the relations between the International Accounting Standards Board (“IASB”) and FASB.⁶ An important argument in the U.S. debate is the idea that IFRS, which are promulgated by the London-based IASB, are dominated by Europeans. In the United States, IFRS are, therefore, often seen as a “Trojan horse” proposed by Europeans (and others) to replace American accounting culture, which is still based on the Generally Accepted Accounting Principles (“GAAP”), promulgated by the FASB. To slightly exaggerate the argument, IFRS are seen as an effort of the European accounting tradition to colonize the United States with an allegedly inferior set of accounting standards.⁷ This view is bolstered by the fact that the SEC

Bumps, CPA J. (Oct. 2006), available at <http://www.nysscpa.org/cpajournal/2006/1006/essentials/p36.htm> (discussing “challenging hurdles . . . [on] the road to convergence for the United States and Europe via IFRS”).

⁶ United Nations Conference on Trade and Development, *Practical Implementation of International Financial Reporting Standards: Lessons Learned*, U.N. Doc. UNCTAD/DIAE/ED/2008/1 (Aug. 2008) (detailing the “unprecedented” spread of IFRS).

⁷ See, e.g., Paul Meller, *International Auditing Rules Urged on U.S.*, N.Y. TIMES, Feb. 22, 2002, at W1 (discussing the increased push by the European Commission for the United States to abandon GAAP following the Enron collapse); Floyd Norris, *The Case for Global Accounting*, N.Y. TIMES, May 11, 2012, at B1 and B6 (outlining the historical and potential development towards a “common set of high-quality accounting standards that applied globally” but noting that “[s]ome Americans argue that accepting international standards would reduce the quality of American financial statements”); Kara Scannell & Joanna Slater, *SEC Moves to Pull Plug on U.S. Accounting Standards*, WALL ST. J., Aug. 28, 2008, at A1 (comparing GAAP with IFRS and outlining problems with implementing IFRS within the United States); Charles Niemeier, Bd. Member, Pub. Co. Acct. Oversight Bd. (PCAOB), Keynote Address on Recent International Initiatives at the 2008 Sarbanes-Oxley, SEC and PCAOB Conference, New York State Society of Certified Public Accountants (Sept. 10, 2008), at 3 (arguing that political pressure from Europe, primarily from Angela Merkel of Germany, is the reason why the United States moved towards IFRS); *Harmonizing Accounting Standards and Auditing Procedures – A Survey*, in 10 INTERNATIONAL CAPITAL MARKETS AND SECURITIES REGULATION 1-117–1:130.2 (Harold S. Bloomenthal & Samuel Wolff eds., 2003) (arguing that the EU was pushing the United States to accept financial statements prepared by EU firms in accordance with IFRS, and that the SEC found itself “between a rock and a hard place”); James E. Rogers, *Going Too Far Is Worse than Not Going Far Enough: Principle-Based Accounting Standards, International Harmonization, and the European Paradox*, 27 HOUS. J. INT’L L. 429, 451 (2005) (arguing that IAS are similar to British and other European principles of accounting and very different from those of the United States); Robert Bruce, *Now How Does It All Fit Together?*, FIN. TIMES, Sept. 15, 2003, at 1 (outlining difficulties with harmonizing, including that “[i]nternational standards are based on principles and guidance. U.S. standards are based on detailed rulebooks.”); Cunningham, *supra* note 2, at 15 (arguing that the EU was pressuring the SEC on the adoption of IFRS); Neal F. Newman,

permitted foreign issuers to use IFRS largely because of pressure from the EU Commission.⁸ Nevertheless, in this article, we suggest that this perception is a myth. In fact, IFRS have rather been an element of Anglo-American accounting culture, developed with the support of FASB, that Continental European countries have been encouraged, and ultimately forced, to accept by way of the EU with encouragement from the United States. In other words, IFRS have been the Trojan horse of the United States that had and still has to overcome a significant level of resistance in Europe.

The goal of our article is to counter the majoritarian view by shedding light on the purpose and origins of IFRS, and to draw possible lessons from the “internationalization” of accounting standards applicable to publicly traded European firms. While these firms are required by EU law to use IFRS in their consolidated accounts, we show that IFRS developed out of an accounting tradition similar to the United States that is firmly rooted in the approach to capital markets and financial reporting found in the English-speaking world. Both U.S. GAAP and IFRS share a common basis: the assumption that the purpose of public accounting is to provide a useful basis for decision-making by participants in capital markets.

This situation was not the case in Continental Europe before the 1990s, where other purposes such as taxation and creditor protection played key roles. The objections to IFRS in Continental Eu-

The U.S. Move to International Accounting Standards – A Matter of Cultural Discord – How Do We Reconcile?, 39 U. MEM. L. REV. 835, 868–72 (2009) (comparing the United States with Germany and suggesting that Germany is a better fit for IFRS than the U.S.); Karthik Ramanna, *The International Politics of IFRS Harmonization*, 3 ACCT. ECON. & L. 1, 9–12 (2013) (seeing IFRS as a product of the EU and considering it reasonable to treat the EU, including Britain, as a common accounting jurisdiction backing IASB).

Interestingly, IFRS are often defined as “the European ‘equivalent’ of U.S. GAAP.” See, e.g., John Armour, Gérard Hertig & Hideki Kanda, *Transactions with Creditors*, in THE ANATOMY OF CORPORATE LAW 115, 126 (Reinier Kraakman et al. eds., 2d ed. 2009) (quoting European Commission, DG Internal Market and Services Working Document: *Report on Convergence Between International Financial Reporting Standards (IFRS) and Third Country National Generally Accepted Accounting Principles (GAAPs) and on the Progress Towards the Elimination of Reconciliation Requirements that Apply to Community Issuers Under the Rules of These Third Countries* (2008), [available at http://ec.europa.eu/internal_market/accounting/docs/equivalence_report_en.pdf](http://ec.europa.eu/internal_market/accounting/docs/equivalence_report_en.pdf)).

⁸ Roberta S. Karmel, *The EU Challenge to the SEC*, 31 FORDHAM INT’L L.J. 1692, 1704–5 (2008).

rope were far more severe than the ones brought in the United States today. European accounting since the 1970s has been characterized by the European Economic Community (now European Union) Accounting Directives, which set forth a supranational framework for national accounting laws and standards. However, these directives had many gaps and created intended and unintended options that were effectively used by the Member States to maintain their previous accounting systems, which were often very different from those of the United States or the United Kingdom. Thus, IFRS faced considerable resistance when they were initially introduced in Continental Europe, and some issues have still not been fully resolved. We focus in particular on France and Germany, whose accounting traditions had originally inspired the directives. German accounting standard setting was institutionally very different from both U.S. GAAP and IFRS, given that accounting was not primarily governed by standards set by an accounting standard-setter but by statutes that were interpreted as such. Their purposes were also historically different, an important emphasis being on creditor protection and taxation. With the possible introduction of International Accounting Standards (IAS) looming on the horizon in the late 1990s, there was an enormous debate on how to best reconcile these goals with the capital-market-oriented “Anglo-Saxon” accounting. Similarly, in France government actors’ influence on the accounting standard setting process was considerable. IFRS—like U.S. GAAP—are frequently criticized for only taking the interests of investors on the capital markets into account. French standards, in this view, were subject to a process that took the interests of a wider set of corporate stakeholders into account. The changeover to IFRS can thus be seen as a larger element of a transition toward Anglo-Saxon corporate governance practices that is still encountering resistance.

In a number of key EU countries, including these two, the use of IFRS is still limited to consolidated accounts, and primarily to those of publicly traded firms. Traditional domestic accounting standards tend to remain in parallel use for the financial statements of other entities, as well as for the entity-level accounting even of publicly traded firms. Convergence in accounting has, therefore, remained superficial.

Paradoxically, most of the arguments in the United States against IFRS today relate to how the standards are supposedly an accounting system emerging from a foreign legal system that would provide a bad fit for the U.S. economy and its legal and cor-

porate governance environment. As our article demonstrates, these arguments are false. Culturally, economically, and legally, the U.S. capital market is much closer to the biotope from which IFRS developed than is Continental Europe. Since other countries had to make much greater strides, we argue that the purported hurdles in the United States should be considered comparatively unimportant and rather easy to overcome. Moreover, given the historical support of IFRS from the United States and capital market actors in the Anglosphere in general, the SEC's present reticence to endorse IFRS is almost surprising. Now that the U.S. has helped to foist an accounting tradition it shares on everyone else, it is surprising that the country itself would not embrace IFRS. We discuss whether a changeover would lead to substantive changes in accounting, and what implications the inevitable institutional changes would have, looking at various possible policy strategies for the future.

The article proceeds as follows. Section 2 gives an overview of the current debate in the United States and discusses the objections currently brought in the U.S. against the introduction of IFRS. Section 3 looks at the implementation of IFRS in the EU and discusses hurdles they had and still have to face in these countries. We focus on the institutional and historical context of the EU Accounting Directives and accounting standard-setting, as well as the function of accounting in Germany and France. Section 5 uses this comparative account to suggest that the problems in the United States are relatively small and should, therefore, in theory, be easier to overcome. Section 5 concludes.

2. THE U.S. DEBATE ABOUT THE INTRODUCTION OF IFRS

2.1. FASB-IASB Relations over the Past Decade

Up to around 2000, policymakers in the United States and the SEC were confident that U.S. GAAP were the best available accounting standards in the world.⁹ However, the Enron scandal in

⁹ See, e.g., Cunningham, *supra* note 2, at 8 (citing GARY JOHN PREVITS & BARBARA DUBIS MERINO, *A HISTORY OF ACCOUNTANCY IN THE UNITED STATES: THE CULTURAL SIGNIFICANCE OF ACCOUNTING* (rev. ed. 1998)) (explaining that with the rise of globalization, the U.S.'s generally accepted accounting principles

2001 and other subsequent scandals shook the confidence in the U.S. GAAP and accelerated the discussions about whether IFRS, supposedly based more strongly on principles as opposed to rules, would be more successful in preventing frauds in financial reporting.¹⁰

In 2002, Section 108(d) of the Sarbanes-Oxley Act required the SEC to conduct a study and report to the Congress on the adoption of a principles-based accounting system. The report submitted in July 2003 concludes that global accounting standardization would produce merit benefits such as:

- i. greater comparability for investors across firms and industries globally,
- ii. a more efficient allocation by markets of scarce capital among investment alternatives, and

("GAAP") was "commonly reference as the gold standard"); Lisa M. Brown, *United States Accounting Standards: Do the SEC Requirements Regarding U.S. GAAP Violate GATS?*, 28 N.C. J. INT'L L. & COM. REG. 1007, 1019 (2003) (summarizing arguments in favor of retaining GAAP); Bernard Colasse, *Harmonisation Comptable Internationale : De la résistible ascension de l'IASC/IASB*, GERER & COMPRENDRE, Mar. 2004, at 30, 34-35 (suggesting that in the early 1990s Americans no longer saw the need to support IOSCO/IASC because foreign firms were adopting U.S. GAAP voluntarily); Arthur Goldgaber, *Global Investing: How to Research Foreign Companies to Find Opportunities*, SEEKING ALPHA (July 16, 2013, 12:09 PM), <http://seekingalpha.com/article/1550862-global-investing-how-to-research-foreign-companies-to-find-opportunities> (referring to the "transparency" of GAAP and concerns about reliance on foreign accounting standards in relation to U.S. investors investing overseas); Edward F. Greene, Daniel A. Braverman & Sebastian R. Sperber, *Hegemony or Deference: U.S. Disclosure Requirements in the International Capital Markets*, 50 BUS. LAW. 413, 429-30 (1995) (summarizing arguments in favor of retaining GAAP); George Mundstock, *GAAP Did Their Job During the Economic Meltdown*, 4 FIU L. REV. 463, 470-71 (2009) (arguing "GAAP have done well. They are the best accounting standards in the world today GAAP should continue in effect for United States businesses.") (footnote omitted).

¹⁰ Sarbanes Oxley Act of 2002, Pub. L. No. 107-204, § 108(d) (2002) (requiring the SEC to "conduct a study on the adoption by the United States financial reporting system of a principles-based accounting system"); Financial Supervision and Crisis Management in the EU, EU Econ. & Scientific Policy Dept., EUR. PARL. STUDY IP/A/ECON/IC/2007-069 (2007) (by Kern Alexander et al.), available at <http://www.europarl.europa.eu/activities/committees/studies/download.do?language=en&file=26588> (analyzing changes in financial markets and institutions over the past three decades and outlining the consequences of these changes); John C. Coffee, Jr. & Hillary A. Sale, *Redesigning the SEC: Does the Treasury Have a Better Idea?*, 95 VA. L. REV. 707, 749-59 (2009) (reviewing the literature outlining the "principles versus rules debate"); John C. Coffee, Jr., *Understanding Enron: "It's About the Gatekeepers, Stupid,"* 57 BUS. LAW. 1403, 1416-17 (2002) (discussing models of reform following Enron); Lawrence M. Gill, *IFRS: Coming to America*, J. ACCT. (June 2007) (familiarizing American accountants with IFRS).

iii. lower costs of capital, since global accounting standards would eliminate the duplicate cost of preparing two sets of financial statements, and make it easier for companies to have access to capital in other markets.¹¹

In the same year, the 2002 Norwalk Agreement between FASB and IASB showed that the United States was committed to the goal of “the development of high-quality, compatible accounting standards that could be used for both domestic and cross-border financial reporting.”¹² The February 2006 Memorandum of Understanding issued by FASB and IASB laid down specific milestones to be reached by 2008.¹³ Subsequent revisions brought the two sets of standards closer to each other.¹⁴ In 2007, the SEC dropped the

¹¹ Office of the Chief Accountant, SEC, Study Pursuant to Section 108(d) of the Sarbanes-Oxley Act of 2002 on the Adoption by the U.S. Financial Reporting System of a Principles-Based Accounting System (July 25, 2003) [hereinafter SEC Study 2003], *available at* <http://www.sec.gov/news/studies/principlesbasedstand.htm> (outlining the results of the study into a standard setting required under the Sarbanes-Oxley Act).

¹² The Norwalk Agreement, The Financial Accounting Standards Board (FASB) & The International Accounting Standards Board (IASB), Sept. 18, 2002 [hereinafter Norwalk Agreement], *available at* <http://www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175819018817&blobheader=application%2Fpdf> (discussing the method of achieving compatibility between FASB and IASB); *see also* Letter from David Schraa, Director, Regulatory Affairs Dep’t., Institute of Int’l Finance, Inc., to the Securities and Exchange Commission, *available at* <http://www.sec.gov/comments/s7-13-07/s71307-82.pdf> (detailing written comments from the Institute of International Finance, concerning the SEC’s Proposed Rule “Acceptance From Foreign Private Issuers of Financial Statements Prepared in Accordance With International Financial Reporting Standards Without Reconciliation to US GAAP . . .”).

¹³ For a discussion on FASB/SEC interactions with IFRS and strengthening the influence of FASB on IASB standard making process, *see generally* Luzi Hail, Christian Leuz & Peter Wysocki, *Global Accounting Convergence and the Potential Adoption of IFRS by the U.S. (Part II): Political Factors and Future Scenarios for U.S. Accounting Standards*, 24 ACCT. HORIZONS 567 (2010).

¹⁴ BRUCE MACKENZIE, TAPIWA NJIKIZANA, DANIE COE TSEE, RAYMOND CHAMBOKO, AND BLAISE COLYVAS, WILEY IFRS 2011: INTERPRETATION AND APPLICATION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS (2011) [hereinafter WILEY IFRS 2011]; Larson & Street, *supra* note 5 (discussing the “road to convergence” between the United States and EU); *see also* FASB, Completing the February 2006 Memorandum of Understanding: A Progress Report and Timetable for Completion (Sept. 2008), *available at* <http://www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175819018778&blobheader=application%2Fpdf> (outlining the progress of FASB and IASB toward the goals of the Norwalk Agreement, *supra* note 12, and providing a timetable for completion).

“reconciliation to U.S. GAAP” requirement for foreign companies reporting in a manner fully compliant with IFRS as issued by IASB.¹⁵ This decision, while politically driven by pressure from the EU,¹⁶ was widely seen as an acknowledgement by the SEC that IFRS constituted a fully acceptable set of “high quality financial reporting standards.”¹⁷ This change constitutes considerable progress from the perspective of foreign companies listed in the United States, which considered it costly and confusing to have two different financial statements for the same year.¹⁸

The elimination of the reconciliation requirement permitted scholars to compare the value relevance of IFRS-based and U.S.-GAAP-based accounting information by looking at the relation between accounting information and stock market values.¹⁹ Some

¹⁵ Acceptance from Foreign Private Issuers of Financial Statements Prepared in Accordance with International Financial Reporting Standards Without Reconciliation to U.S. GAAP, Security Act Release No. 8879, Exchange Act Release No. 57026, 17 C.F.R. pts. 210, 230, 239 (Dec. 21, 2007) [hereinafter SEC Release, Dec. 21, 2007], available at <http://www.sec.gov/rules/final/2007/33-8879.pdf> (amending rules to allow foreign private investors to prepare SEC filings in accordance with IFRS without reconciliation to GAAP); Press Release, SEC, SEC Takes Action to Improve Consistency of Disclosure to U.S. Investors in Foreign Companies (Nov. 15, 2007), available at <http://www.sec.gov/news/press/2007/2007-235.htm> (summarizing the effect of the SEC rule amendments in 17 C.F.R. pts. 210, 230, 239, and 24); CPA Letter, SEC Eliminates Reconciliation Requirement for Foreign Companies; AICPA Recommends SEC Use International Accounting Standards (recommending international accounting standards) (Jan. 1, 2008), available at http://www.ifrs.com/updates/aicpa/SEC_Eliminates_Reconciliation.html.

¹⁶ Karmel, *supra* note 8, at 1694, 1704–05.

¹⁷ WILEY IFRS 2011, *supra* note 14. This is not the only acknowledgment on that matter. For example, on Feb. 24, 2010, the SEC issued a release expressing its continued support for the convergence of U.S. GAAP and IFRS. See Commission Statement in Support of Convergence and Global Accounting Standards, Security Act Release No. 9109, Exchange Act Release No. 61578, available at <http://www.sec.gov/rules/other/2010/33-9109.pdf>.

¹⁸ See James D. Cox, *Coping in a Global Marketplace: Survival Strategies for a 75-Year-Old SEC*, 95 VA. L. REV. 941, 985 (2009) (“[I]t quite likely was a wise choice for the SEC to cast aside the need for foreign issuers to reconcile their financial statements to GAAP, provided they employ high-quality IFRS for their financial reporting. The reconciliations were months late so that the report that mattered was their earlier-released IFRS-based financial reports.”) (footnote omitted); Larson & Street, *supra* note 5, at 9 (“[I]t is up to each company to choose whether it wishes to issue another set of accounts as well as accounts based upon endorsed IAS, for instance using full IAS or US GAAP.”).

¹⁹ See, e.g., Robert W. Holthausen & Ross L. Watts, *The Relevance of the Value-Relevance Literature for Financial Accounting Standard Setting*, 31 J. ACCT. & ECON. 3 (2001) (evaluating the inferences drawn from value relevance studies); see also Mary E. Barth, William H. Beaver & Wayne R. Landsman, *The Relevance of the Value-Relevance Literature for Financial Accounting Standard Setting: Another View*, 31 J.

found positive or mixed results, while others found no evidence of change.²⁰ Although it may still be necessary to find a better way to evaluate the switch,²¹ today, 450 companies using IFRS are listed in the U.S. report, with an aggregate market capitalization exceeding five trillion dollars.²²

Overall, the 2007 decision of the SEC was welcomed by many with the hope that U.S. capital markets would regain competitiveness as compliance with SEC regulations would become easier and less costly.²³ At that time, the argument was that U.S. capital markets had become less likely to attract foreign issuers because of excessive regulation, including the requirement of filing financial reports according to U.S. GAAP.²⁴ The study of the Committee on

ACCT. & ECON. 77 (2001) (explaining that value relevance studies adequately and accurately assess accounting information); Ahsan Habib, *Legal Environment, Accounting Information, Auditing and Information Intermediaries: Survey of the Empirical Literature*, 26 J. ACCT. LIT. 1, 13-18 (2007) (arguing that value-relevance of a country's accounting information is dependent on that country's legal system); Wayne R. Landsman, Edward L. Maydew & Jacob R. Thornock, *The Information Content of Annual Earnings Announcements and Mandatory Adoption of IFRS*, 53 J. ACCT. & ECON. 34 (2012) (suggesting that the significance of accounting depends on the strength of legal enforcement in the respective country).

²⁰ See, e.g., Tzu-Ting Chiu & Yen-Jung Lee, *Foreign Private Issuers' Application of IFRS Around the Elimination of the 20-F Reconciliation Requirement*, 48 INT'L J. ACCT. 54, 57 (2013) (finding that accounting data under IFRS and U.S. GAAP are of similar quality, but that quality is reduced by reconciliation); John (Xuefeng) Jiang et al., *Did Eliminating the 20-F Reconciliation Between IFRS and U.S. GAAP Matter?* 1-32 (Michigan State University, Working Paper, 2010) (finding no evidence that reconciliation is associated with abnormal trading volume or return volatility); Yongtae Kim, Haidan Li & Siqi Li, *Does Eliminating the Form 20-F Reconciliation from IFRS to U.S. GAAP Have Capital Market Consequences?*, 53 J. ACCT. & ECON. 249 (2011) (finding no evidence of a negative impact on market liquidity or cost of equity).

²¹ See Muhammad Jahangir Ali, *A Synthesis of Empirical Research on International Accounting Harmonization and Compliance with International Financial Reporting Standards*, 24 J. ACCT. LITERATURE 1, 44 (2005) (discussing difficulty of reconciling accounting standards across nations).

²² See Hans Hoogervorst, Tokyo Speech: Defining Profit or Loss and OCI...Can It Be Done? (Feb. 5, 2014) (finding that most of the foreign companies in the United States reported using IFRS since 2007).

²³ See, e.g., Christopher Hung Nie Woo, *United States Securities Regulation and Foreign Private Issuers: Lessons from the Sarbanes-Oxley Act*, 48 AM. BUS. L.J. 119, 121 (2011) ("While U.S. securities laws should be reformed to decrease the risk of, and mitigate the effects of, future financial crises, absent a global harmonized regulatory regime, the United States should be careful to minimize the costs imposed by U.S. securities regulation on foreign private issuers.").

²⁴ See Cox, *supra* note 18 (discussing decision by SEC that allows non-convergence by foreign companies); Roberta S. Karmel & Claire R. Kelly, *The Hardening of Soft Law in Securities Regulation*, 34 BROOK. J. INT'L L. 883, 909 (2009)

Capital Markets Regulation found that “[f]oreign companies are not only choosing to stay away from the U.S. public market, those that have come are leaving.”²⁵ Yet, the decision seems not to have strongly affected the competitiveness of U.S. markets. If anything, the number of foreign issuers newly listed in the U.S. slightly decreased since 2007, although the decision to cross-list is driven by a variety of factors, including the financial crisis.²⁶

In 2008, when the global financial crisis highlighted the interdependence of global financial markets, the leaders of the G20 called for global accounting standards, and urged FASB and IASB to complete their convergence projects by 2011.²⁷ For many, the introduction of IFRS in the U.S. seemed inevitable in today’s global capital markets.²⁸

(explaining that the SEC “set forth a ‘roadmap’ for eliminating the need for non-U.S. companies to reconcile to U.S. GAAP financial statements prepared according to IFRS” in response to the international shift toward IFRS and the threat of multinational corporations leaving the U.S. to raise capital in the growing European and Asian markets, because of their uniform use of IFRS); Donald C. Langevoort, *U.S. Securities Regulation and Global Competition*, 3 VA. L. & BUS. REV. 191, 192 (2008) (discussing the effect of the financial meltdown on economic activity shifting away from the United States); Larson & Street, *supra* note 5 (discussing “challenging hurdles” on “the road to convergence for the United States and Europe via IFRS”); Woo, *supra* note 23, at 121 (suggesting that the United States should be cautious in implementing IFRS in relation to foreign private issuers); Scannell & Slater, *supra* note 7, at A1 (noting that political pressure from Germany is possible explanation for why the United States moved towards IFRS).

²⁵ *The Competitive Position of the U.S. Public Equity Market*, COMM. ON CAP. MKTS. REG. (2007), www.capmksreg.org/press/the-competitiveness-position-of-the-u-s-public-equity-market/; see also Woo, *supra* note 23, at 130–34 (“[A]ccounting and disclosure appear to be the biggest costs for most foreign private issuers.”).

²⁶ See *Annual Query Tool*, WORLD FED’N OF EXCHANGES, <http://www.world-exchanges.org/statistics/annual-query-tool> (last visited Sept. 24, 2014) (explaining that in 2007, seventy-four foreign companies were newly listed either in NYSE or NASDAQ. After the financial crisis, there was a sharp decline in the newly listed companies. For instance, there were only thirty-two newly listed companies in 2008. Most recently, sixty-two new foreign companies were listed in 2011).

²⁷ See Declaration, G20 Summit on Financial Markets and the World Economy (Nov. 15, 2008) [hereinafter 2008 Summit], <http://g20.org/images/stories/docs/eng/washington.pdf> (declaring a joint collaboration to encourage global economic growth); Leaders’ Statement, The Pittsburgh Summit (Sept. 24–25, 2009) [hereinafter 2009 Summit], https://www.g20.org/sites/default/files/g20_resources/library/Pittsburgh_Declaration_0.pdf (reaffirming the G20 Washington Summit in 2008).

²⁸ See William W. Bratton & Lawrence A. Cunningham, *Treatment Differences and Political Realities in the GAAP-IFRS Debate*, 95 VA. L. REV. 989 (2009) (highlighting the complications that can arise with switching to IFRS despite the benefits of incorporating it); Moritz Pöschke, *Incorporation of IFRS in the United States: An*

The same year, FASB and IASB agreed on a “Roadmap” for potential use of IFRS by U.S. issuers and targeted a successful convergence between IFRS and U.S. GAAP.²⁹ It underlines the point that, as trading and investment become more global, investors face an increasing need for disclosure that facilitates comparison of financial information across investment alternatives in different parts of the world.³⁰ Organizations such as the G20 and AICPA had concluded that IFRS provide the best available set of global accounting standards,³¹ and the SEC seemed set to achieve convergence by 2011, and adoption by 2014.³²

However, when Mary Shapiro took office as the SEC chair in 2009, she declared that the move towards IFRS, “if it were to occur,” should take place more slowly than had previously been indicated.³³ In line with this, the SEC’s April 2011 Progress Report

Analysis of the SEC’s Options and the Implications for the EU, 9 EUR. CO. & FIN. L. REV. 51 (2012) (analyzing the effects of the SEC switching to IFRS); Sharda Sharma, *The Impact of the Adoption of International Financial Reporting Standards on the Legal Profession*, 10 HOUS. BUS. & TAX J. 139 (2010) (describing the impact that the inevitable implementation of IFRS will have on the legal profession in the United States); Stephen A. Zeff, *IFRS Developments in the USA and EU, and Some Implications for Australia*, 18 AUSTL. ACCT. REV. 275 (2008) (“The US has already taken a long stride towards joining the more than 110 countries and other jurisdictions that have committed themselves to allow or require the use of IFRS for some or all reporting entities.”).

²⁹ SEC Roadmap, Nov. 14, 2008, *supra* note 4 (discussing the creation of a roadmap to allow the implementation and use of IFRS in the United States for the purpose of SEC filings).

³⁰ *Id.* (“U.S. investors would benefit from an enhanced ability to compare financial information of U.S. companies with that of non-U.S. companies.”).

³¹ 2009 Summit, *supra* note 27 (finding that IFRS provides the best global accounting standards); *see also* PWC, IFRS AND U.S. GAAP: SIMILARITIES AND DIFFERENCES 3 (2011) (comparing IFRS and U.S. GAAP accounting standards); Harvey Goldschmid, Keynote Address at IFRS Foundation/AICPA Conference in Boston: U.S. Incorporation of IFRS is a National Imperative (Oct. 5-7, 2011) (stating that the goal of a single set of high quality global accounting standards is important for the SEC, and this, realistically, can only be IFRS); Ervin Black, Greg Burton & Spencer Paul, *US Perspectives on Implementation of IFRS, in LAW, CORPORATE GOVERNANCE, AND ACCOUNTING: EUROPEAN PERSPECTIVES* 19, 19 (Victoria Krivogorsky ed., 2011) (finding IFRS to be “uniquely positioned” to fill the need for globally accepted accounting principles).

³² SEC Roadmap, Nov. 14, 2008, *supra* note 4 (noting that in November 2008, the SEC proposed making a decision in 2011 to mandate IFRS adoption with a planned phase-in of adoption dates—2014 for larger accelerated filers, 2015 for mid-sized companies, and 2016 for small companies).

³³ Questions from Senator Carl Levin for Mary Schapiro, Nominee to Be Chair of the Securities & Exchange Commission (Jan. 8, 2009), *available at* <http://levin.senate.gov/imo/media/doc/supporting/2009/PSI.SchapiroRespons>

disclosed that the two Boards had extended the timetable for the convergence projects “beyond June 2011 to permit further work and consultation with stakeholders.”³⁴ The first half of 2012 was targeted for the completion according to the press release of the projects, and a decision on the specific date for mandatory IFRS for U.S. companies was expected thereafter. However, to date, there is still no definite decision as to “whether, when, and how the current financial reporting system for U.S. issuers should be transitioned to a system incorporating IFRS.”³⁵ While the Final Staff Report of the SEC had been expected to make a clear recommendation, the report failed to recommend the endorsement of IFRS or even provide a timeline.³⁶ In spite of widespread frustration with this situation among EU policymakers,³⁷ the SEC is still not sure whether the U.S. will move forward with IFRS, as it is not even clear whether the two boards will be able to reach convergence on the key aspects of *all* projects.³⁸

2.2. *Objections to the Adoption of IFRS*

While the SEC is committed to the goal of a single set of global

es.012209.pdf.

³⁴ IASB and FASB, *Progress Report on IASB-FASB Convergence Work* (Apr. 21, 2011), available at <http://www.fasb.org/cs/BlobServer?blobkey=id&blobwhere=1175822338795&blobheader=application%2Fpdf&blobcol=urldata&blobtable=MungoBlobs> (noting that “the boards extended the timetable for the remaining priority MoU convergence projects and insurance beyond June 2011” and discussing reasons for the delay in convergence).

³⁵ See SEC Staff Paper, May 26, 2011, *supra* note 4, at 1 (discussing how to incorporate IFRS in the United States).

³⁶ See SEC Final Staff Paper, July 13, 2012, *supra* note 4 (failing to make a clear recommendation or endorsement for a financial reporting system).

³⁷ See Olivier Guersent, Address at Conference EFRAG/Trustees: An EU Perspective on the Move Towards Global Accounting Standards (Oct. 11, 2012) (citing frustration with the U.S.’ failure to commit to or endorse IFRS); Press Release, European Financial Reporting Advisory Group (EFRAG), An EU Perspective on the Move Towards Global Accounting Standards (Oct. 16, 2012) (“European Commission representatives expressed disappointment with financial reporting developments in the U.S. and made clear that frustration in the EU was growing.”).

³⁸ See SEC Final Staff Paper, July 13, 2012, *supra* note 4; SEC Staff Paper, May 26, 2011, *supra* note 4, at 8 (“[I]n the event that the Commission determines to incorporate IFRS, the Staff envisions that FASB would remain the standard-setting body responsible for promulgating U.S. GAAP under the framework.”).

accounting standards,³⁹ it seems reluctant to take the next step and set a date for adoption. Once the EU persuaded the SEC to allow foreign companies to use IFRS when they are listed in the U.S., the expectation was that convergence between EU and the U.S. securities regulations would quickly spread to other areas, including allowing U.S. listed companies to use IFRS.⁴⁰ However, recent developments imply that there will be no “big bang approach” and the SEC might come up with “ways that a softer transition or change over time can occur.”⁴¹ The following sections explore several reasons that seem to underlie the SEC’s ambivalent stance. The first set of concerns address procedural issues relating to the introduction of IFRS. The sheer size of the U.S. economy and the possibly disastrous consequences, both nationally and internationally, of a rushed decision may be one reason (section 2.2.1.).⁴² Moreover, we discuss the objection that it might not be legitimate for the SEC to delegate accounting standard setting to an *international* body (section 2.2.2.). The second and more important set of concern relates to the substance of IFRS. U.S. GAAP currently follow a “rules-based” model, while the IFRS model is purportedly “principles-based.” Detractors of the IFRS have argued that this and other features of IFRS will make them less useful in the U.S. economic and legal setting. Section 2.2.3. introduces the debate, and section 2.2.4. discusses how it may be linked to peculiar aspects of U.S. legal culture, in particular investor litigation.

³⁹ See Press Release, SEC, SEC Approves Statement on Global Accounting Standards (Feb. 24, 2010), available at <http://sec.gov/news/press/2010/2010-27.htm> (stating that the SEC is committed to one accounting standard); see also SEC Work Plan, Feb. 24, 2010, *supra* note 4 (asserting the SEC’s commitment to a global accounting standard).

⁴⁰ Karmel, *supra* note 8, at 1694, 1712.

⁴¹ See Ken Tysiac, *Beswick: “Change Fatigue” a Barrier to IFRS in U.S.*, J. ACCT., May 2, 2013 (discussing the SEC’s lack of action towards incorporating the IFRS).

⁴² See Goldschmid, *supra* note 31 (suggesting that the Dodd-Frank Act will not be a reason for a delay). But see Michael Cohn, *AICPA to Reconsider IASB Recognition, Definition of Attest, and Global Credentials*, ACCT. TODAY (May 13, 2013) (noting that the SEC is understaffed, and that SEC Chair Mary Jo White has indicated that Dodd-Frank and the JOBS Act are priorities).

2.2.1. Too Big to Fail: The U.S. Economy and the Role of the SEC

Most obviously, the SEC appears reluctant to abandon American exceptionalism in accounting due to the fact that the U.S. is the largest economy in the world. Given the high stakes, the SEC may reasonably want to be cautious about moving forward while making sure that IFRS succeed in the long run.⁴³ A premature adoption of a set of underdeveloped accounting standards might have severe consequences around the world, given the role of the well-developed U.S. public equity market in providing external finance to foreign companies.⁴⁴ Metaphorically speaking, for a “large vessel” such as the U.S. financial system, it may be simply more difficult to get back on the right course after a wrong (or even disastrous) one has been set.

Moreover, because of the large size of the U.S. capital market, possible benefits from adopting IFRS will likely be less substantial than in smaller markets. One of the standard rationales for mandatory financial disclosure of publicly traded firms is that information is a public good whose benefits the issuer does not fully internalize.⁴⁵ In part, the reason for this is network effects resulting from investors comparing different firms.⁴⁶ Within the U.S., these

⁴³ See, e.g., Cunningham, *supra* note 2, at 64–65 (“Of note, it is not evident from official SEC documents or Commissioner speeches that the agency fully appreciates IASB’s fragility.”); see also Ken Tysiac, *Beswick: Rule-making Preventing SEC from Deciding on IFRS*, J. ACCT. (Dec 9, 2013) (explaining that the SEC is hesitant to change quickly over to IFRS, and that a gradual change is preferred).

⁴⁴ Luzi Hail, Christian Leuz & Peter Wysocki, *Global Accounting Convergence and the Potential Adoption of IFRS by the U.S. (Part I): Conceptual Underpinnings and Economic Analysis*, 24 ACCT. HORIZONS 355, 366–68 (2010) (providing a detailed discussion on costs and benefits of IFRS adoption in the US).

⁴⁵ Gerard Hertig, Reinier Kraakman & Edward Rock, *Issuers and Investor Protections*, in THE ANATOMY OF CORPORATE LAW 275, 276–281 (2d ed., Reinier Kraakman et al. eds., 2009); Allen Ferrell, *The Case for Mandatory Disclosure in Securities Regulation around the World*, 2 BROOK. J. CORP. FIN. & COM. L. 81 (2007) (discussing effects of mandatory disclosure regulations across the globe); see also Allen Ferrell, *Mandatory Disclosure and Stock Returns: Evidence from the Over-the-Counter Market*, 36 J. LEGAL STUD. 213 (2007) (discussing mandatory disclosure requirements on publicly traded companies more generally); Holger Daske, Luzi Hail, Christian Leuz & Rodrigo Verdi, *Mandatory IFRS Reporting Around the World: Early Evidence on the Economic Consequences*, 46 J. ACCT. RES. 1085 (2008) (examining the effects of mandatory IFRS).

⁴⁶ See Karthik Ramanna & Ewa Sletten, *Network Effects in Countries’ Adoption of IFRS* (Harvard Bus. Sch. Working Paper, Paper No. 10-092), available at <http://ssrn.com/abstract=1590245> (describing the hypothesis that worldwide

network effects may be large enough because of the sheer market volume.⁴⁷ In smaller markets, these benefits may only materialize if investors are capable of diversifying across a set of exchanges, for which a single set of accounting standards may be required as a basis.⁴⁸

It is of course true that the New York Stock Exchange (NYSE) is the largest stock market in the world by market capitalization. As of December 2011, its equity market capitalization was 11.8 billion dollars, followed most closely by the domestic equity markets of Tokyo and London with 3.3 billion dollars each.⁴⁹ However, there are a number of objections to this argument. In a globalized world, capital markets are perhaps not best seen in national terms. Collectively, the countries using IFRS constitute a larger economy than the United States, with a market capitalization exceeding that of the U.S. exchanges by more than a quarter.⁵⁰ In the United States, the number of publicly traded firms has decreased since the mid-1990s,⁵¹ and there have been few IPOs since the dot-com bubble

IFRS acceptance is self-reinforcing, due in large part to network benefits such as lower transaction costs).

⁴⁷ *Id.* at 5 (“Larger countries, due to the size of their markets, are likely to attract foreign capital and maintain international trade even if they continue using domestic standards.”).

⁴⁸ *See, e.g.,* Ramanna & Sletten, *supra* note 46, at 5, 6, 30 (explaining that smaller markets may experience limited market benefits from IFRS); Hail et al., *supra* note 44, at 364–66 (“[T]here is evidence of positive capital market outcomes around the IFRS mandates in some countries. However, there is considerable heterogeneity in the effects across firms and countries.”).

⁴⁹ *WFE 2011 Market Highlights*, WORLD FED’N OF EXCHANGES (Jan. 19, 2012), available at <http://www.world-exchanges.org/files/file/stats%20and%20charts/2011%20WFE%20Market%20Highlights.pdf> (analyzing financial market trends across the globe).

⁵⁰ Christopher Cox, Chairman, U.S. Securities and Exchange Commission, Speech at Open Meeting in Washington, D.C. (Aug. 27, 2008), available at <http://www.sec.gov/news/press/2008/2008-184.htm> (stating that market capitalization in 85 countries requiring IFRS represented approximately 35% of global market capitalization in July 2008, which exceeded the 28% share of U.S. exchanges).

⁵¹ *WFE Statistics: 10 Years in Review, 2000–2009*, WORLD FED’N OF EXCHANGES, available at www.world-exchanges.org (summarizing market capitalization and value of share trading over 2000–2009); David Weild & Edward Kim, *A Wake-Up Call for America*, in GRANT THORNTON: CAPITAL MARKETS SERIES (Nov. 2009), available at http://www.gt.com/staticfiles/GTCom/Public%20companies%20and%20capital%20markets/gt_wakeup_call_.pdf (discussing the decline in the number of publicly listed companies in the United States and its economic impact on the econo-

burst.⁵² Some firms have permanently left the market, and international issuers have increasingly sought listings elsewhere, e.g., in London.⁵³ Accounting standards may therefore be a competitive factor for the U.S. stock market, and particularly for American firms seeking both domestic and international investment.

Since the formation of FASB in the early 1970s, U.S. issuers believed that U.S. GAAP was well developed and perfectly met the needs of U.S. business and its investors and thus provided American firms with a competitive edge.⁵⁴ In spite of incidents such as the Enron scandal, the SEC held on to the belief that this system generally works well. The purpose of adopting IFRS would therefore not primarily be to remedy the defects of the existing system, but rather to harmonize U.S. accounting practices with those used in the rest of the world, and thus help the U.S. capital market, and U.S. firms, to regain international competitiveness. In addition, adopting IFRS in the United States may facilitate U.S. public companies' access to international capital.⁵⁵

Harmonization may be desirable if the goal for SEC is to protect U.S. investors investing globally, and to secure a strong position for the United States in today's competitive global capital markets,⁵⁶ whereas keeping U.S. specific financial reporting stand-

my); see also Alix Stuart, *Missing: Public Companies: Why is the Number of Publicly Traded Companies in the U.S. Declining?*, CFO.COM (Mar. 22, 2011), <http://ww2.cfo.com/growth-companies/2011/03/missing-public-companies/> (describing the general decrease in U.S. publicly traded companies).

⁵² *The Competitive Position of the U.S. Public Equity Market*, *supra* note 25 ("U.S. exchanges have captured just 13.8% of the total value of Global IPOs in 2007, compared with an average of 74% in the period from 1996 to 2000.").

⁵³ SOX has often been blamed for this. See, e.g., Langevoort, *supra* note 24, at 195 (describing the expanding geographic reach of U.S. investors); Newman, *supra* note 7, at 839 ("The United States is no longer the preferred choice for raising capital. Today, companies can raise needed capital just as easily in London, Hong Kong, or Dubai rather than New York.").

⁵⁴ See Stephen A. Zeff, *The Evolution of U.S. GAAP: The Political Forces Behind Professional Standards*, CPA J. (Feb. 2005) (providing a historical overview).

⁵⁵ See Langevoort, *supra* note 24, at 195 ("In the years since [2001], the world's major wealth gains have not occurred in real economic activity in the United States"); Newman, *supra* note 7, at 842-61 (comparing differences between GAAP and IFRS); Ken Tysiac, *IFRS Foundation Report Says SEC's Concerns Can Be Overcome*, J. ACCT. (Oct. 23, 2012) (IFRS chairman addresses U.S. concerns over shift to new standards).

⁵⁶ See Tysiac, *supra* note 55 ("[T]he United States could face consequences for not pushing steadily forward on convergence and adopting IFRS."); Cunningham, *supra* note 2, at 21 ("Evidence demonstrates increasing divergence rather than convergence between IFRS and U.S. GAAP"); Langevoort, *supra* note 24, at 195 (ar-

ards may end up being the major barrier to the integration of financial markets.⁵⁷ As former SEC Chair Christopher Cox said in 2008, “two thirds of U.S. investors own securities issued by foreign companies.”⁵⁸ Thus, “[a] common accounting language around the world could give investors greater comparability and greater confidence in the transparency of financial reporting worldwide.”⁵⁹ International harmonization of financial reporting standards allows governments to develop standards that keep investors informed in a uniform way and across borders.⁶⁰ In other words, both American investors and issuers should be able to benefit from amplified network effects if the financial reporting landscape of the United States were integrated into the developing global one, in which investors are able to compare financial statements of firms worldwide using a single set of standards.

2.2.2. *Delegating Authority to a Private International Body*

Another concern also debated in the EU has been about “ratifying as laws the set of rules created by a small, self-appointed, private-sector body.”⁶¹ However, it is hard to justify such an argument in the United States, as the constitutional structures and decision-making processes of FASB and IASB are almost identi-

guing that companies are already raising capital, not just in New York but all around the world, including London, Hong Kong, and Dubai); Newman, *supra* note 7, at 835 (“Convergence is, from the accounting and financial reporting world’s viewpoint, the single most important thing in the history of the world.”).

⁵⁷ WALTER MATTLI & TIM BÜTHE, *THE NEW GLOBAL RULERS: THE PRIVATIZATION OF REGULATION IN THE WORLD ECONOMY* 197 (2013).

⁵⁸ Tysiac, *supra* note 55 (“[T]he United States’s contributions are lacking in proportion to the size of its economy and its number of representatives in IFRS Foundation bodies.”); *see also* Cunningham, *supra* note 2, at 21 (noting that differences between IFRS and U.S. GAAP continue to grow); Langevoort, *supra* note 24, 195 (arguing that U.S. access to international capital and economic growth suffered possibly as a result of U.S. regulation); Newman, *supra* note 7, at 835 (emphasizing that convergence is fundamentally important).

⁵⁹ SEC Roadmap, Nov. 14, 2008, *supra* note 4 (discussing a plan that allows the use of IFRS by U.S. issuers for the purpose of SEC filings).

⁶⁰ MATTLI & BÜTHE, *supra* note 57, at 197.

⁶¹ *See* Wiley IFRS 2011, *supra* note 14, at 20 (noting that IFRS achieved legal force in the EU only when the European Council of Ministers approved the IFRS Regulation in June 2002); Bratton & Cunningham, *supra* note 28, at 1000–01 (summarizing various criticisms of FASB’s governance model).

cal.⁶² Many describe the extent of the similarity as IASB being the “carbon copy” of FASB—only on a broader geographic scale.⁶³ FASB has been the standard-setter in the United States since 1973, and is a private body, as were its predecessors. Since the 1930s, the Commission has been relied on as an independent, private-sector organization to establish accounting standards, which apparently never caused debate about the legitimacy of private standard-setting.⁶⁴ In fact, only the Sarbanes-Oxley Act of 2002 created an explicit authority for the SEC to recognize a private standard-setting body and set up criteria for recognition,⁶⁵ but the private character of accounting standards was never an issue. Hence, the concern obviously originates not from the fact that IASB is a *private* standard-setter, but from the fact that it is a *foreign* one.

The United States is often reluctant to espouse foreign and international standards. The U.S. Supreme Court is divided on the question of “whether it is legitimate to rely on foreign law”⁶⁶—

⁶² Bratton & Cunningham, *supra* note 28, at 1000–01 (noting that FASB’s governance model has been replicated by IASB); see David S. Ruder, Charles T. Canfield & Hudson T. Hollister, *Creation of World Wide Accounting Standards: Convergence and Independence*, 25 NW. J. INT’L L. & BUS. 513, 526–40 (2005) (noting that the overhaul of IASB’s structure in 2000 was motivated by the desire to follow the American model and thus facilitate the adoption of IFRS in the United States).

⁶³ William W. Bratton, *Headless Globalism: The SEC’s Roadmap to Accounting Convergence*, 79 U. CIN. L. REV. 471, 476 (2010) (using the “carbon-copy” language and noting only two points of distinction—money and public oversight—between IASB and FASB); Ruder, Canfield & Hollister, *supra* note 62, at 540–54 (describing the ways in which IASB, prior to its reorganization in 2000, differed from FASB).

⁶⁴ See generally *Facts About FASB*, FIN. ACCT. STANDARDS BD., <http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176154526495> (last visited Oct. 9, 2014) (describing that the Financial Accounting Foundation, founded in 1972, is a private-sector organization overseeing FASB, which was established by the FAF in 1973. Accounting Standards codified by FASB are officially recognized as authoritative by the SEC (Financial Reporting Release No. 1, Section 101, and reaffirmed in its April 2003 Policy Statement) and the American Institute of Certified Public Accountants; Rule 203, Rules of Professional Conduct, as amended May 1973 and May 1979).

⁶⁵ Sarbanes-Oxley Act of 2002, § 108(a), 15 U.S.C. § 7218 (2002) (recognizing accounting standards set by private standard-setting bodies when they meet certain additional requirements).

⁶⁶ Martin Gelter & Mathias M. Siems, *Language, Legal Origins, and Culture Before the Courts: Cross-Citations Between Supreme Courts in Europe*, 21 SUP. CT. ECON. REV. 215, 220 (2013) (demonstrating that citation of foreign law by courts in the United States is not an isolated phenomenon); see also *Roper v. Simmons*, 543 U.S. 551 (2005) (ruling that it is unconstitutional to impose the death penalty on juvenile offenders); *Lawrence v. Texas*, 539 U.S. 558 (2003) (making same-sex sexual activity legal in the United States); *Foster v. Florida*, 537 U.S. 990 (2002) (ruling that a defendant cannot be sentenced to death without considering mitigating cir-

even though foreign and international law are cited only as a secondary (nonbinding) sources (i.e., at the same level as law review articles).⁶⁷ Justice Scalia, possibly the most outspoken opponent of the practice, argues in one of his decisions, “this Court . . . should not impose foreign moods, fads, or fashions on Americans.”⁶⁸

From not ratifying even the basic international human rights agreements such as the Convention on the Elimination of All Forms of Discrimination Against Women (“CEDAW”),⁶⁹ and the U.N. Convention on the Rights of the Child,⁷⁰ to arguing the legitimacy of citing international or foreign decisions and laws, when it comes to following foreign/international legal developments, “imposing foreign moods . . . on Americans”⁷¹ seems to be a major

cumstances); *Atkins v. Virginia*, 536 U.S. 304 (2002) (ruling that executions of mentally retarded criminals violate the Eighth Amendment).

⁶⁷ See Ruth Bader Ginsburg, *Looking Beyond Our Borders: The Value of a Comparative Perspective in Constitutional Adjudication*, 22 *YALE L. & POL'Y REV.* 329, 331 (2004) (noting that some jurists “adhere to the view that a comparative perspective . . . is inapplicable to [the Constitution’s] interpretation” but urging the American Constitutional Society to incorporate international perspectives in their understanding of the Constitution); see also Jess Bravin, *Looking Global: Ginsburg Speaks Out on Kagan, Comparative Law Issue*, *WALL ST. J.*, July 30, 2010, <http://blogs.wsj.com/law/2010/07/30/looking-global-ginsburg-speaks-out-on-kagan-comparative-law-issue/> (supporting the claim that judicial reference to foreign and international law is not unprecedented in the United States).

⁶⁸ Gelter & Siems, *supra* note 66, at 5 (citing *Lawrence v. Texas*, 539 U.S. 586, 598 (2003) (Scalia, J., dissenting)).

⁶⁹ CEDAW is an international agreement that affirms principles of fundamental human rights and equality for women around the world that was adopted by the United Nations General Assembly in 1979. All but seven countries – the U.S., Iran, Sudan, South Sudan, Somalia, Palau, and Tonga – have ratified the treaty. United Nations Convention on the Elimination of All Forms of Discrimination Against Women, Dec. 18, 1979, 1249 U.N.T.S. 13, available at http://treaties.un.org/Pages/ViewDetails.aspx?src=TREATY&mtdsg_no=IV-8&chapter=4&lang=en. See *CEDAW: U.S. Ratification and Local Implementation Efforts*, *BERKELEY LAW SCH.*, available at <http://www.law.berkeley.edu/8285.htm>, for a description of efforts within the U.S. to ratify CEDAW; see also *Women Senators Made the CEDAW Connection to Ending Violence Against Women and Girls, CEDAW at a Glance* (June 26, 2014), <http://www.cedaw2010.org> (describing efforts by U.S. Senators to ratify CEDAW).

⁷⁰ United Nations Convention on the Rights of the Child (UNCRC), Nov. 20, 1989, 1577 U.N.T.S. 3 (a human rights treaty setting out the civil, political, economic, social, health and cultural rights of children. Since its adoption in 1989, the Convention has become the most widely ratified human rights treaty in history. Only two countries, Somalia and the United States, have not ratified the treaty).

⁷¹ *Lawrence v. Texas*, 539 U.S. at 598 (Scalia J., dissenting) (quoting *Foster v. Florida*, 537 U.S. 990 (2002) (Thomas, J., concurring in denial of certiorari)) (arguing that the Court’s discussions of foreign views on sodomy are not only meaningless but also dangerous dicta).

concern in the U.S.⁷² CEDAW and the U.N. Convention on the Rights of the Child are not the only examples. The United States has so far signed hundreds of treaties but has not ratified them.⁷³ Arguably, harmonization in many fields has so far been possible only when the Europeans give in, but, more often than not, the United States subsequently does not apply those standards.⁷⁴

The skepticism U.S. judges, scholars, and politicians have regarding foreign law is not the only instance we see U.S. exceptionalism. Rather, it is part of a larger pattern that includes the refusal to adopt the metric system⁷⁵ and the use of the term "soccer" for the game known to the rest of the world as "football."

Clearly, IASB is not completely foreign in the sense of excluding U.S. representation. Thus, the actual fear in the United States may be that the United States would be *underrepresented* in the new regime. Against this fear must be balanced other countries' concerns that the United States, which has still not adopted IFRS but is in the position to influence IASB substantially, is actually *overrepresented* in the current regime.

The fear of delegating authority over financial reporting to a non-U.S. organization has grown so much by now that some have

⁷² See, e.g., 151 CONG. REC. S3, 109 (daily ed. Mar. 20, 2005) (statement of Sen. Cornyn) (arguing that citation of foreign law implies that the American people are "losing control over the meaning of our laws and of our Constitution"); Martha Minow, *The Controversial Status of International and Comparative Law in the United States*, 52 HARV. INT'L L.J. ONLINE 1, 1-2 (2010) available at http://www.harvardilj.org/2010/08/online_52_minow/ ("locating the sources of the controversy over the place of international law within the United States" in order to "dismiss artificial issues" and focus on "developments that might be instructive").

⁷³ Curtis A. Bradley, *Unratified Treaties, Domestic Politics, and the U.S. Constitution*, 48 HARV. INT'L L.J. 307, 309-10 (2007) (describing the large number of treaties that the United States has signed but not subsequently ratified, which include humanitarian, environmental, and private international law treaties, among others); see, e.g., Guri Bang, *Signed But Not Ratified: Limits to U.S. Participation in International Environmental Agreements*, 28 REV. POL'Y RES 65 (2011) (exploring two distinct explanations for why the United States signs environmental treaties but does not ratify them); see also Mara E. Trager, *Towards a Predictable Law on International Receivables Financing: The UNCITRAL Convention*, 31 N.Y.U. J. INT'L L. & POL. 611, 614, 637-38 (1999) (noting that the Anglo-American and Continental European big-law systems try to impose the law of their countries on others, making reaching a consensus more difficult if not impossible).

⁷⁴ See Trager, *supra* note 73, at 625 (establishing the three different trans-border transactions that might be covered by the draft rules).

⁷⁵ See Ramanna, *supra* note 7, at 35 (noting that besides the United States, only Liberia and Myanmar have eschewed the metric system).

started to question the authority of the SEC to decide on such delegation.⁷⁶ However, the SEC clearly stated that it has the authority and has been delegating its power to FASB since the 1970s. Furthermore, should the SEC decide to adopt IFRS, FASB will remain the body responsible for endorsing international standards, which would be a precondition for their application in the United States.⁷⁷

The influence of the United States on the emergence of IFRS dates back to before its foundation. The predecessor of the current IFRS Foundation,⁷⁸ the International Accounting Standards Committee Foundation (“IASC Foundation”) was formed in 1973, through an agreement among nine national accounting bodies: Australia, Canada, France, Germany, Japan, Mexico, Holland, the United Kingdom, and the United States.⁷⁹ Arguably, the Anglo-

⁷⁶ See, e.g., Interview by Sen. Carl Levin with Mary Schapiro, Nominee to be Chair of the Securities and Exchange Commission (Jan. 8, 2009), <http://www.levin.senate.gov/imo/media/doc/supporting/2009/PSI.SchapiroResponses.012209.pdf> (asking whether the Sarbanes-Oxley Act allows “the SEC to delegate the development of U.S. accounting standards to the IASB”); Jacob L. Barney, Note, *Beyond Economics: The U.S. Recognition of International Financial Reporting Standards as an International Subdelegation of the SEC’s Rulemaking Authority*, 42 VAND. J. TRANSNAT’L L. 579 (2009) (questioning the SEC’s authority to recognize standard-setters besides FASB); see also Cunningham, *supra* note 2, at 28–33 (arguing that the SEC’s authority to recognize standard-setters besides FASB is suspect). But see Sarbanes-Oxley Act, *supra* note 10, § 108 (reaffirming the SEC’s role in establishing accounting standards to be used by public companies); *infra* § 4.2.1. (discussing the SEC’s authority and suggesting an endorsement approach as a possible solution).

⁷⁷ SEC Roadmap, Nov. 14, 2008, *supra* note 4, at 1 (proposing a roadmap to allow the use of IFRS by U.S. issuers for the purpose of the SEC filings); see Stephen A. Zeff & Christopher W. Nobes, *Commentary: Has Australia (or Any Other Jurisdiction) ‘Adopted’ IFRS?*, 20 AUSTL. ACCT. REV. 178, 178–84 (2010) (analyzing the various methods that jurisdictions can use to implement IFRS). For additional discussion on who actually adopted IFRS in a way that each standard is effective as soon as it is issued by IASB, see *infra* § 4.2.1.

⁷⁸ IFRS, *IASC Foundation to Become IFRS Foundation on 1 July 2010*, IFRS.ORG, (June 30, 2010), <http://www.ifrs.org/news/announcements-and-speeches/Pages/Announcements-and-Speeches.aspx> (follow “Next” hyperlink to June 30, 2010) (noting that on July 1, 2010, the IASC Foundation formally renamed itself as International Financial Reporting Standards Foundation (IFRS Foundation)); IFRS FOUNDATION, CONST., preface at 4 (Jan. 2013) (amending the Constitution “to reflect the separation of the role of the Chair of the IASB from that of the Executive Director.”).

⁷⁹ See CLARE ROBERTS, PAULINE WEETMAN & PAUL GORDON, *INTERNATIONAL FINANCIAL REPORTING: A COMPARATIVE APPROACH* 331 (3d ed. 2005) (reflecting on the changes within international accounting standards); Mark J. Hanson, *Becoming One: The SEC Should Join the World in Adopting the International Financial Reporting Standards*, 28 LOY. L.A. INT’L & COMP. L. REV. 521, 521–23 (2006) (noting that many countries already use or will use IFRS and questioning whether the SEC can cur-

Saxon countries dominated.⁸⁰

The “three-tier governance structure” of IFRS is similar to the U.S. model of FASB. First, IASB consists of fifteen independent experts, four of whom are American. Second, five out of the twenty-two Trustees of the IFRS Foundation are from the United States. Third, the Monitoring Board is made up of five securities regulators including the SEC.⁸¹ In other words, U.S. influence is perceptible at all levels of the institutional structure associated with the IFRS. In addition to all these structural similarities, IASB’s standards have gradually been amended in the course of a deliberate process to create convergence with GAAP. The FASB-IASB joint project has resulted in changes both in U.S. GAAP and IFRS to the extent that they are now “far more similar than they are different.”⁸² In fact, IFRS mirror U.S. GAAP in many respects.⁸³

rently adopt IFRS for foreign issuers); WILEY IFRS 2011, *supra* note 14, at 7 (describing the structure of the IASC Foundation); CHRISTOPHER NOBES & ROBERT PARKER, *COMPARATIVE INTERNATIONAL ACCOUNTING* 85 (12th ed. 2012).

⁸⁰ Leo van der Tas & Peter van der Zanden, *The International Financial Reporting Standards*, in *THE INFLUENCE OF IAS/IFRS ON THE CCCTB, TAX ACCOUNTING, DISCLOSURE AND CORPORATE LAW ACCOUNTING CONCEPTS* 1, 3 (Peter Essers et al. eds., 2009) (discussing the significant consequences that the introduction of IAS/IFRS might have); Alain Burlaud & Bernard Colasse, *Normalisation comptable internationale: le retour du politique ?*, 16 *COMPTABILITE CONTROLE AUDIT* 153, 155-56 (2010) (pointing out that four former English colonies—and only one other country—joined in 1974).

⁸¹ Goldschmid, *supra* note 31, at 8 (describing the ways in which the “three-tiered governance model” of IFRS mirrors the U.S. FASB and noting that the similarities are deliberate).

⁸² Stuart H. Deming, *International Financial Reporting Standards: Their Importance to U.S. Business and Legal Practice*, 84 *MICH. BAR J.* 14, 17 (Dec. 2005) (discussing how the United States will have to adapt its accounting standards to the international accounting standards now prominent among other nations); *see generally* SEC Staff Paper, Nov. 16, 2011, *supra* note 4 (providing examples of recent changes to FASB and/or IASB standards as a result of joint projects).

⁸³ *See, e.g.*, SEC Staff Paper, Nov. 16, 2011, *supra* note 4, at 5 (noting that IFRS 10 resulted in “substantial convergence of IFRS with U.S. GAAP on structural investment vehicles and other special purpose entities as well as related disclosures . . .”). For a more detailed discussion on Consolidation and SPEs, *see* § 2.2.3. Another example of substantially converged standards is IFRS 3. *See* SEC Staff Paper, Nov. 16, 2011, *supra* note 4, at 6, 44-45 (noting that both IFRS 3 and ASC Topic 805 contain similar requirements for business combinations accounting and noncontrolling interests).

2.2.3. *The Rules-Principles Debate in Accounting*

While procedural obstacles should normally be only temporary, substantive objections to IFRS should play a role in the debate irrespective of the cost of transition. This kind of objection does not concern specific details, but rather the nature of this set of standards as a whole and its purported incompatibility with the U.S. financial reporting environment and the legal system as a whole.⁸⁴

The main critique relates to the level of detail of the two sets of accounting standards.⁸⁵ It is often claimed that U.S. GAAP are rule-based, while IFRS are principles-based.⁸⁶ These two terms used by accountants are more or less analogous to what legal scholars mean when they set up a dichotomy of “rules” and “standards.”⁸⁷ In the accounting context, a rules-based approach means that a particular statement gives relatively detailed instruc-

⁸⁴ Newman, *supra* note 7, at 840–41 (arguing that the U.S.’s “shareholder demographic” and “corporate culture” fit poorly with the “principle-based tenants” of IFRS); see Shyam Sunder, *IFRS and the Accounting Consensus*, 23 ACCT. HORIZONS 101, 101 (2009) (arguing for a re-examination of the accounting consensus).

⁸⁵ E.g., Bratton, *supra* note 63, at 489–90 (discussing some of the negative impacts of FASB rules); Newman, *supra* note 7, at 844–45 (pointing out that U.S. GAAP have a larger volume of information, totaling approximately 4,530 pages, than do IFRS with 2,719 pages).

⁸⁶ SEC Staff Paper, Nov. 16, 2011, *supra* note 4, at 9–11 (analyzing the text of IFRS as issued by IASB as compared to the text of U.S. GAAP); see, e.g., INST. OF CHARTERED ACCT. AUSIL., *SEC Progress on U.S. IFRS Adoption*, CHARTEREDACCOUNTANTS.COM.AU (Sept. 2, 2014), <http://www.charteredaccountants.com.au/Industry-Topics/Reporting/Current-issues/Convergence/News-and-updates/SEC-progress-on-US-IFRS-adoption.aspx> (announcing the SEC’s completion of two key phases of its work plan toward adopting IFRS in the U.S.).

⁸⁷ See Louis Kaplow, *Rules Versus Standards: An Economic Analysis*, 42 DUKE L.J. 557 (1992) (“offer[ing] an economic analysis of the extent to which legal commands should be promulgated as rules or standards”); Duncan Kennedy, *Form and Substance in Private Law Adjudication*, 89 HARV. L. REV. 1685, 1685–1713 (1976) (“address[es] the problem of the choice between rules and standards” at Sections I and II); see, e.g., William W. Bratton, *Enron, Sarbanes-Oxley and Accounting: Rules Versus Principles Versus Rents*, 48 VILL. L. REV. 1023, 1030 (2003) (looking at Enron as an example of governance breakdown and audit failures); Lance J. Phillips, *The Implications of IFRS on the Functioning of the Securities Antifraud Regime in the United States*, 108 MICH. L. REV. 603, 616–18 (2010) (explaining how “investors and the Securities and Exchange Commission will face greater difficulty in relying on accounting violations to establish the elements of the securities antifraud causes of action if IFRS is adopted”).

tions regarding specific accounting treatment to be given to particular transactions.⁸⁸ Under a principles-based approach, the applicable accounting standard applies to a more general set of transactions, which consequently requires the accountant to employ greater discretion to comply with a general objective such as fair presentation.⁸⁹

For example, accounting for leases is often used to illustrate the difference between the two systems because the accounting treatment (i.e., an operating lease or a capital lease) determines whether the corporation should report the lease as an asset or as an expense.⁹⁰ U.S. GAAP employ bright line criteria, such as requiring "seventy-five percent or more of the leased property's economic life . . ." to determine when the transaction will be recorded as a capital lease instead of an operating lease.⁹¹ In spite of requiring a similar treatment of accounting for leases, IFRS do not provide quantified measures and state the idea in principled terms. IAS 17 requires capital lease accounting if "the lease term is for the major part of the economic life of the asset." IFRS require preparers to understand the essence of the transaction and report on its substantive reflection, while U.S. GAAP are more prescriptive and try to be as clear as possible.

Another important example is consolidation⁹²—more precisely,

⁸⁸ Phillips, *supra* note 87, at 616–17 (explaining the differences between GAAP and IFRS); *see also* Bratton, *supra* note 87, at 1037 (arguing that our corporate governing system is not yet ready for principles-based accounting because of incentive problems).

⁸⁹ Phillips, *supra* note 87, at 617–18 (asserting that because IFRS lacks guidance, it requires managers to use "estimates, assumptions, and judgment calls"); Bratton, *supra* note 87, at 1036–37 (arguing that the use of principles allows regulators more leeway in applying law to fact, but suggesting the principles can be manipulated by non-neutral regulators).

⁹⁰ Newman, *supra* note 7, at 845–50 (explaining the differences and similarities between U.S. GAAP and IFRS); Bratton & Cunningham, *supra* note 28, at 994 (establishing GAAP as rules-based and IFRS as principles-based); Bratton, *supra* note 63, at 479 (discussing the obstacles of implementing IFRS effectively in the U.S., as it is more "an international focal point around which a broad range of national systems converge as national regulators adopt IFRS with local carve outs" than it is a national system in itself).

⁹¹ Newman, *supra* note 7, at 849 (describing similarities and differences in the accounting treatment for leases under GAAP and IFRS); FIN. ACCT. STANDARDS BD., STATEMENT OF FINANCIAL ACCOUNTING STANDARDS NO. 13: ACCOUNTING FOR LEASES ¶ 7 (1976) (describing criteria for classifying leases other than leveraged leases).

⁹² Bratton & Cunningham, *supra* note 28, at 994–95 (establishing GAAP as rules-based and IFRS as principles-based); *see* Bratton, *supra* note 63, at 479–80

accounting for Special Purpose Entities (“SPEs”)—and when to report SPEs on a consolidated basis. Debate about this issue erupted shortly after the Enron scandal, when a partnership controlled by Enron’s CFO was used to circumvent consolidation requirements and thus effectively shift some corporate debt off the books.⁹³ Critics argued that a more principles-based approach would have prevented Enron from employing such tactics, since it would not have been possible to simply claim to have followed the rules while avoiding compliance with the more general objective of accounting standards to consolidate all entities under the *de facto* control of the reporting entity.⁹⁴ Others objected that Enron did not follow U.S. GAAP to the letter.⁹⁵ Yet, the criticism persuaded Congress to (leg-

(describing cases in which GAAP is known for its rules and IFRS for its principles, including accounting for capital leases and accounting consolidation).

⁹³ JOHN C. COFFEE, JR., GATEKEEPERS: THE PROFESSIONS AND CORPORATE GOVERNANCE 22–23 (2006); see *U.S. v. Arthur Andersen*, 374 F.3d 281, 284 (5th Cir. 2004) (explaining how Enron created special purpose entities to engage in off-balance-sheet transactions and affirming the district court holding convicting Arthur Andersen of obstructing SEC proceedings). However, with *Arthur Andersen v. U.S.*, 544 U.S. 696, 696–98 (2005), the Supreme Court reversed the charges against Arthur Andersen. The Supreme Court decision did not declare the auditing firm was innocent but merely found the jury instructions were erroneous. Even the Supreme Court decision overturning the charges could not save the company from dissolution as its reputation was already damaged irreparably by then.

⁹⁴ Coffee, *supra* note 10, at 1416–17 (2002); Bratton, *supra* note 87, at 1026 (characterizing the “principles-based accounting and “international convergence” of GAAP as being within the “institutional contexts in which they would operate and effect consequences” and determining that its principles-based accounting presents risks for audit quality); see Joel S. Demski, *Enron et al. – A Comment*, 21 J. ACCT. & PUB. POL’Y 129, 129–30 (2002) (discouraging a rush into new regulatory structures and encouraging a retreat from bright line reporting); Mark Nelson, John Elliott & Robin Tarpley, *Evidence from Auditors About Managers’ and Auditors’ Earnings Management Decisions*, 77 ACCT. REV. 175 (2002) (reporting “analyses of data obtained using a field-based questionnaire in which 253 auditors from one Big Five firm recalled and described 515 specific experiences they had with clients whom they believe[d] were attempting to manage earnings”).

⁹⁵ See, e.g., David Kershaw, *Evading Enron: Taking Principles Too Seriously In Accounting Regulation*, 68 MOD. L. REV. 594, 616–24 (2005) (comparing pre-Enron and post-Enron accounting standards); Coffee, *supra* note 93, at 24 (arguing that Enron’s incentives to manage for the short-term ultimately led to the crimes committed); Bratton, *supra* note 87, at 1041–43 (arguing that while the GAAP’S rules with respect to accounting were “poorly drafted and incomplete, it was Enron’s strategic decision to evade the rules that led to the scandal, not any failure in the rules themselves); Cunningham, *supra* note 2, at 17 (arguing that in contrast to the suggestion that GAAP’s rules were written in such a way as to lead Enron into

islatively) commission (in the Sarbanes-Oxley Act of 2002) an SEC report on whether the United States should adopt a principles-based accounting system.⁹⁶

Before Enron, the test corporations reporting under U.S. GAAP were required to simply state whether they were “holding majority voting control over the affiliate.”⁹⁷ The standard FASB enacted on that matter in 2003⁹⁸ is less specific, and it broadened the previous criterion, which merely required voting control over SPEs.⁹⁹ The new standard requires a company to consolidate if “a company is exposed to a majority of an entity’s expected losses or entitled to a majority of entity’s residual returns.”¹⁰⁰ Arguably, the new criterion is more open-textured—and thus more principles-based—than the prior one.¹⁰¹ Still, the applicable IFRS on consolidation¹⁰² pro-

demise, it was actually Enron’s blatant decision to evade the rules of GAAP that led to the scandal).

⁹⁶ SEC Study 2003, *supra* note 11 (outlining the results of the study into standard setting required under the Sarbanes-Oxley Act).

⁹⁷ Coffee, *supra* note 93, at 22–24 (analyzing the impact of Enron’s failures); Newman, *supra* note 7, at 853–58 (explaining the differences between U.S. GAAP and IFRS as seen through their approaches to consolidation); FIN. ACCT. STANDARDS BD., STATEMENT OF FINANCIAL ACCOUNTING STANDARDS NO. 94: CONSOLIDATION OF ALL MAJORITY OWNED SUBSIDIARIES ¶¶ 6–7 (1987) (noting that businesses use “nonhomogeneity” as grounds to exclude majority owned subsidiaries from consolidation); *see also* Kershaw, *supra* note 95, at 607 (discussing possible ambiguities in a consolidation standard based on voting control).

⁹⁸ FIN. ACCT. STANDARDS BD., FASB INTERPRETATION NO. 46, CONSOLIDATION OF VARIABLE INTEREST ENTITIES: AN INTERPRETATION OF ARB NO. 51, 1, 1–49 (2003) (addressing consolidation of business enterprises of variable interest entities possessing certain characteristics); Newman, *supra* note 7, at 853–58 (explaining the differences between U.S. GAAP and IFRS as seen through their approaches to consolidation).

⁹⁹ Newman, *supra* note 7, at 853–58 (explaining the differences between U.S. GAAP and IFRS as seen through their approaches to consolidation).

¹⁰⁰ *Id.* at 854; *see* FASB INTERPRETATION NO. 46, *supra* note 99 (describing consolidation of business enterprises); Newman, *supra* note 7, at 853–58 (describing how Financial Interpretation 46(R)’s consolidation model, the variable interest model, has enlarged SPE consolidation in order to prevent the kind of financial maneuvering that occurred with Enron); *see also* SEC, OFFICE OF THE CHIEF ACCOUNTANT, REPORT AND RECOMMENDATIONS PURSUANT TO SECTION 401(C) OF THE SARBANES-OXLEY ACT OF 2002 ON ARRANGEMENTS WITH OFF-BALANCE SHEET IMPLICATIONS, SPECIAL PURPOSE ENTITIES, AND TRANSPARENCY OF FILINGS BY ISSUERS 91 (2003) (a study conducted by the SEC addressing “two primary questions: (1) the extent of off-balance sheet (“OBS”) arrangements, including the use of special purpose entities (“SPEs”), and (2) whether current financial statements of issuers transparently reflect the economics of off-balance sheet arrangements”).

¹⁰¹ Newman, *supra* note 7, at 854–55 (discussing Financial Interpretation 46R and its implications of corporate consolidation of SPEs).

vides even less specific guidance about whether to consolidate an SPE.¹⁰³ A reporting entity must consolidate an investee when the former controls the latter. Arguably, the reporting entity and its auditor need to exercise a greater degree of judgment under IFRS 10.¹⁰⁴ In order to eliminate inconsistencies, IFRS 10 articulates the principle of control in such a way that it can be applied to all investees. Under this standard, control consists of three elements: power, exposure to variable returns, and an investor's ability to use power to affect its amount of variable returns.¹⁰⁵

If a purportedly "principles-based" approach could solve America's accounting woes, why would anyone object? In spite of these examples, the established dichotomy is often considered problematic.¹⁰⁶ Clearly, it does not imply that U.S. GAAP do not employ any principles, or that IFRS exclusively consist of principles. To the contrary, U.S. GAAP and IFRS each combine both.¹⁰⁷ It may be true that the IFRS include fewer specific rules because

¹⁰² INT'L ACCT. STANDARDS BD., IFRS 10 CONSOLIDATED FINANCIAL STATEMENTS (2011). IFRS 10—Consolidated Financial Statements supersedes IAS 27—Consolidated and Separate Financial Statements and SIC-12—Consolidation, Special Purpose Entities. See IFRS Foundation, Effect Analysis: IFRS 10 *Consolidated Financial Statements* and IFRS 12 *Disclosure of Interests in Other Entities* (Sept. 2011, updated Jan. 2012) [hereinafter IFRS Foundation, Effect Analysis] (observing several causes of inconsistent application of IAS 27 and SIC-12 that have resulted in diversity in practice and thus resulting in the issuance of IFRS 10).

¹⁰³ Newman, *supra* note 7, at 856 (discussing the IFRS accounting consolidation regime for SPEs and noting that it is based on the "broader and more complex idea of control").

¹⁰⁴ IFRS Foundation, Effect Analysis, *supra* note 102, at 22, 33, 39, 44 (outlining substantive rights for investors); Newman, *supra* note 7, at 855–56 (noting that issuers must use greater judgment and discretion under the principles-based IFRS standards when determining whether to consolidate a group of SPEs).

¹⁰⁵ IFRS Foundation, Effect Analysis, *supra* note 102, at 8 (explaining the principle of control and its elements in detail).

¹⁰⁶ See Phillips, *supra* note 87, at 616 n.100 (describing the dichotomy between rules and standards); Russell B. Korobkin, *Behavioral Analysis and Legal Form: Rules vs. Standards Revisited*, 79 OR. L. REV. 23, 30 (2000) (questioning the dichotomy between rules and standards).

¹⁰⁷ See SEC Study 2003, *supra* note 11 (concluding that the benefits of using objectives-oriented or principles-based standards in the United States are challenging to determine); see Lawrence A. Cunningham, *A Prescription to Retire the Rhetoric of "Principles-Based Systems" in Corporate Law, Securities Regulation, and Accounting*, 60 VAND. L. REV. 1411, 1413 (2007) (explaining how defining a system as principle-based or rule-based may be too narrow); Newman, *supra* note 7, at 845 (describing Professor Cunningham's view that rule-based and principle-based standards are too rigid); see also Bratton, *supra* note 87, at 1026, 1036–55 (explaining that Enron violated both rules and standards under U.S. GAAP).

such rules could create problems in countries with very different economies, while more general prescriptions could be interpreted in ways that would better fit the particular circumstances.¹⁰⁸ For instance, U.S. GAAP include detailed cost and expense guidance for extractive industries (oil and gas), but there is no corresponding guidance under IFRS. While industry-specific standards are an important aspect of the U.S. accounting system, IASB has not followed in FASB's footsteps in this respect,¹⁰⁹ nor is it planning to do so.¹¹⁰ Moreover, even if a system has a larger number of rules than another, this does not make it automatically rules-based, because of the importance of how a specific rule is interpreted and applied against the backdrop of the underlying principles.¹¹¹ As we will discuss below, U.S. GAAP and IFRS are both much more similar to each other than they are to Continental European accounting systems, which often had completely different objectives and were – in a certain way – more principles-based than either of them.

Even if we accept the rules-principles dichotomy as typically presented in the debate, one objection is that a principles-based approach could trigger negative reactions by accountants, auditors, and firms in the United States, who are accustomed to working with bright-line rules rather than principles. They may perceive IFRS's lack of bright-lined rules and detailed guidance as an unwanted complication to the current system of audit and enforcement. For instance, Sunder strongly argues against the implementation of IFRS for several reasons, including that IFRS favor principles instead of detailed rules.¹¹² These principles focus on "fairness" which could only be "an *ex post* judgment about a particular instance of valuation," as opposed to an "*ex ante* judgment."¹¹³ Thus, it is impossible for a standard to "specify the numbers arrived at by the application of a particular method to be 'fair'

¹⁰⁸ See October 2012 IFRS Foundation Report, *supra* note 4, at 9–10 (assessing the differences in comprehensiveness between U.S. GAAP and the IFRS).

¹⁰⁹ See SEC Staff Paper, May 26, 2011, *supra* note 4 (discussing one approach to incorporating IFRS into the U.S. system); SEC Final Staff Paper, July 13, 2012, *supra* note 4 (discussing the Work Plan and how to incorporate IFRS into the U.S. system).

¹¹⁰ See generally October 2012 IFRS Foundation Report, *supra* note 4.

¹¹¹ See Kershaw, *supra* note 95, at 606–08 (discussing the relationship between accounting standards and rule entrenchment).

¹¹² Sunder, *supra* note 84, at 103 (asserting that principles, and not rules, should be used to describe accounting standards).

¹¹³ *Id.*

by definition. . . ."¹¹⁴

Consequently, IFRS allow for greater discretion compared to U.S. GAAP. This seems to be the major concern raised by accountants in the United States, given that discretion increases the risk of opportunistic accounting.¹¹⁵ IFRS focus on fair value measurement has been criticized, as it "significantly impairs the ability of an auditor to limit opportunistic actions of management and improve financial reporting."¹¹⁶ Arguably, by providing principles rather than bright-line rules, IFRS create greater opportunities to engage in "financial engineering" to achieve the desired presentation in the financial statements.¹¹⁷

However, a detailed comparison with U.S. GAAP would not necessarily reveal that the latter standards are indeed better at protecting investors in a public company from managerial misconduct with the help or tacit support of accountants and auditors. Currently, U.S. GAAP are characterized by exceptions to more general rules, and often there are exceptions to these exceptions.¹¹⁸ After Enron, a common criticism has been that the larger number of rules and exceptions makes it even more complicated and harder to track "financial engineering."¹¹⁹ As Goldschmid states,

"[P]rinciples (with enough specificity to create comparabil-

¹¹⁴ *Id.*; see also Kaplow, *supra* note 87, at 560 (offering an economic analysis of rules versus standards, suggesting that the distinction "is the extent to which efforts to give content to the law are undertaken before or after individuals act.").

¹¹⁵ SEC Work Plan, *supra* note 4 (citing various comment letters to the SEC, including those from the American Accounting Association, Financial Accounting Standards Committee ("AAA-FASC"), Fund Stockowners Rights, National Association of State Boards of Accountancy ("NASBA"), and Psoras).

¹¹⁶ *Id.*

¹¹⁷ See WILEY IFRS 2011, *supra* note 14. *But see supra* note 89 (regarding the prevalence of financial engineering).

¹¹⁸ For a detailed discussion on rules and exceptions, see Cass R. Sunstein, *Problems with Rules*, 83 CALIF. L. REV. 953, 962 (1995) ("It is familiar to find rules that have explicit or implicit exceptions for cases of necessity or emergency. It is unfamiliar to find rules without any such exceptions."); see also Lawrence A. Cunningham, *Private Standards in Public Law: Copyright, Lawmaking and the Case of Accounting*, 104 MICH. L. REV. 291, 324 n.169 (2005) (explaining difficulties in accessing FASB materials).

¹¹⁹ *E.g.*, Newman, *supra* note 7, at 878 ("A good crook can outsmart a good cop any day of the week."); Bratton & Cunningham, *supra* note 28, at 1004 ("There is no question that GAAP's layers of rules can have perverse effects. . . . Worse, there results a dysfunctional, check-the-box approach to compliance that admits transaction structuring and other strategic behavior . . .").

ity) can be better applied and enforced than detailed rules with bright lines and multiple exceptions. The modern principle-based approach has been incorporated into IASB/FASB converged standards. It is much harder to defeat—by financial engineering—a well-crafted principle than a detailed, specific rule. The last two decades have taught us that financial types find it much too easy to manipulate and structure their ways around ‘hard and fast’ rules.”¹²⁰

2.2.4. “Vague Principles” and Their Fit with Prevalent Investor Litigation

Scholars such as Newman link the rules-principles dilemma to the “cultural fit” discussion and question whether U.S. issuers have the “proper mindset to apply principles-based standards.”¹²¹ IFRS require issuers to capture the “economic substance” of transactions and to prepare financial statements accordingly. However, Newman claims that U.S. issuers’ intent is “not necessarily to get the numbers ‘right’ but to present their company’s financial position as favorably as possible without running afoul of the accounting guidance in that particular area.”¹²² Without having clear boundaries of right and wrong, it is not apparent whether U.S. issuers would choose the “fair presentation” over “presenting finan-

¹²⁰ Goldschmid, *supra* note 31 (explaining the need for the SEC to make a decision with respect to IFRS incorporation).

¹²¹ Newman, *supra* note 7, at 859 (analyzing the suitability of the United States for adoption of the IFRS); Bratton & Cunningham, *supra* note 28, at 998–99 (explaining how blockholders, such as the United Kingdom, Australia, and Israel experience less problems with respect to agency and informational access); see William W. Bratton, *Rules, Principles, and the Accounting Crisis in the United States*, 5 EUR. BUS. ORG. L. REV. 7 (2004) (demonstrating that the cultural fit discussion was most lively during the acceptance of IAS/IFRS across Europe due to Anglo-American origin of these standards); see also Andreas M. Fleckner, *FASB and IASB: Dependence Despite Independence*, 3 VA. L. & BUS. REV. 275, 299 (2008) (describing how, with respect to the IASC, the European Commission did not want to become a standard-setter).

¹²² Newman, *supra* note 7, at 859 (arguing that U.S. companies’ accounting figures serve the purpose of being the most beneficial to the company while still fitting within the regulatory scheme, rather than trying best to fit into the defined rules).

cial statements as favorably as possible.”¹²³ Newman’s argument lends itself to some obvious criticism. First, other countries have produced their fair share of accounting scandals.¹²⁴ European scandals such as Parmalat have prompted the EU to pass a new Audit Directive in 2006,¹²⁵ and auditing remains high on the Commission’s agenda.¹²⁶ It is not clear why issuers and auditors in the U.S.—a country that scores quite well on corruption indices¹²⁷—should be culturally more susceptible to accounting fraud than others. For the argument to persuade, the opportunities and incentives to publicize misleading financial statements would have to be particularly strong in the United States.

In fact, another concern seems to point in exactly the opposite direction, namely a particularly strong, possibly excessive incentive structure discouraging accounting fraud. It is sometimes argued that “IFRS’s less detailed and prescriptive guidance could

¹²³ *Id.* at 866–67 (explaining that before the U.S. can effectively utilize the less-structured IFRS, it must first address corporations’ reluctance to a principles-based regime); Bratton, *supra* note 121, at 28–30 (arguing that auditors and the accounting industry demand rules because clients require justifications); *see, e.g.*, Woo, *supra* note 23, at 121 (citing SEC Commissioner Kathleen L. Casey noting “that one of the lessons of the current financial crisis is that financial stability depends on investor confidence, which in turn depends on the transparency of financial statements.”).

¹²⁴ *E.g.* John C. Coffee, Jr., *A Theory of Corporate Scandals: Why the United States and Europe Differ*, 21 OXFORD REV. ECON. POL’Y 198 (2005) (comparing U.S. scandals such as Enron and WorldCom with European ones such as Parmalat and Ahold).

¹²⁵ Directive 2006/43/EC of the European Parliament and the Council of 17 May 2006 on Statutory Audits of Annual Accounts and Consolidated Accounts, Amending Council Directives 78/660/EEC and 83/349/EEC and Repealing Council Directive 84/253/EEC, 2006 O.J. (L 157/87).

¹²⁶ In November 2011, the commission issued two further proposals: the Proposal for a Regulation of the European Parliament and of the Council on Specific Requirements Regarding Statutory Audit of Public-Interest Entities, and the Proposal for a Directive of the European Parliament and the Council amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts. *See generally* Proposal for a Regulation of the European Parliament and of the Council on Specific Requirements Regarding Statutory Audit of Public-Interest Entities, COM (2011) 779 final (Nov. 30, 2011); Proposal for a Directive of the European Parliament and of the Council Amending Directive 2006/43/EC on Statutory Audits of Annual Accounts and Consolidated Accounts, COM (2011) 778 final (Nov. 30, 2011).

¹²⁷ For example, Transparency International lists the United States in the nineteenth position on its 2012 corruption index, just behind the United Kingdom and ahead of several Western European countries, including Austria, France, Spain, and Italy. *See Corrupt Perceptions Index 2012*, TRANSPARENCY INT’L, <http://cpi.transparency.org/cpi2012/results/> (lasted visited Oct. 1, 2014) (showing a map of corruption perceptions globally).

expose companies to increased claims by shareholders and others seeking to challenge its application, given the perceived litigious environment in the United States."¹²⁸ Preparers and auditors of financial statements are not comfortable with the possibility that even judgments made in good faith, that seemed reasonable at that time, could be second-guessed in court, in spite of them having asked for assurance from the SEC on that matter.¹²⁹ IFRS require accountants to use more judgment and, while this may have several advantages, might also mean a greater exposure to liability for them.¹³⁰ Some argue that litigation against auditors based on alleged negligence and defending accountants against such suits might result in increased opportunities for lawyers when IFRS are fully adopted.¹³¹ Given that most jurisdictions using IFRS still lack class action suits, extensive discovery, and contingency fees,¹³² litigation risk simply may not be salient outside the United States.

However, class action litigation is extensively used in the United States and, as Woo points out, "in 2004 class action suits cost publicly traded companies in the United States \$4.74 billion, compared with \$40.48 million in the United Kingdom. The fact that the number in the United States is more than one hundred times that

¹²⁸ SEC Work Plan, *supra* note 4, at 7 (citing comment letters from FPL Group, Inc. ("FPL") and tw telecom); see Pöschke, *supra* note 28, at 66–69 (discussing the effects of securities litigations in the United States); Phillips, *supra* note 87, at 608–12 (discussing the role of GAAP violations in securities fraud litigation); Robert M. Bushman & Joseph D. Piotroski, *Financial Reporting Incentives for Conservative Accounting: The Influence of Legal and Political Institutions*, 42 J. ACCT. & ECON. 107, (2006) (exploring how reported accounting figures are shaped by a country's individual regulation scheme).

¹²⁹ SEC Study 2003, *supra* note 11 (explaining the work plan to transition the United States into an IFRS regime); SEC Work Plan, *supra* note 4 (concluding that the benefits of using objectives-oriented or principles-based standards in the United States are challenging to determine).

¹³⁰ See Bratton, *supra* note 121, at 28–30 (arguing that auditors and the accounting industry demand rules because clients require justifications); Cunningham, *supra* note 107, at 1473 (arguing that a principle-based system is needed for a broad regulatory scheme); Newman, *supra* note 7, at 873 (asserting that it is inefficient for GAAP and IFRS to govern accounting principles across the globe).

¹³¹ Thomas C. Pearson, *Potential Litigation Against Auditors for Negligence*, 5 BROOK. J. CORP. FIN. & COM. L. 405 (2011) (arguing that measures should be taken to alleviate the rampant negligence in the auditing field); Sharma, *supra* note 28, at 163 (asserting that a switch to IFRS will likely affect the legal profession).

¹³² E.g. Manning Gilbert Warren III, *The U.S. Securities Fraud Class Action: An Unlikely Export to the European Union*, 37 BROOK. J. INT'L L. 1075, 1083–87 (2012) (discussing reasons why securities class actions are unlikely to spread widely in the EU).

experienced in the United Kingdom is the primary reason the cost of director and officer insurance in the United States is six times greater than in Europe.”¹³³

Although the number of securities class action settlements has decreased significantly in recent years, total settlement dollars in 2012 alone increased by more than 100 percent from 2011.¹³⁴ This mechanism in the United States “has enjoyed considerable success both as a deterrent to large-scale corporate securities fraud and as a source of compensatory recovery for investors.”¹³⁵ According to Warren, its success originates from a “uniquely adversarial legal system in a uniquely litigious culture.”¹³⁶ From a behavioral law and economics perspective, the concern about excessive litigation risk seems at least plausible.

Hindsight bias compounded with the ex-post judgment of an incident under a less detailed, principles-based IFRS may increase the liability risk of companies, accountants, and auditors. According to this concept, defendants are relatively likely to be found liable ex-post because “once something happens, people tend to think it was more likely to occur, and easier to foresee, than it really was.”¹³⁷ For example, jurors of a car accident case are more likely to think that the car accident was foreseeable and that the driver could have prevented it had she been more careful. However, participants in behavioral experiments intended to mimic a jury trial were more reluctant to find a driver negligent because the accident was supposedly foreseeable if conditions (e.g. weather, road) were

¹³³ Woo, *supra* note 23, at 132 (arguing that the U.S. regulatory system should be devised to decrease risk of future decline in order to compete with foreign stock markets).

¹³⁴ The number of securities class action settlements reached a fourteen-year low in 2012, with only fifty-three court-approved settlements. However, the average settlement amount (\$54.7 million) increased more than 150 percent in 2012 from prior years, and this amount is well above the historical average (\$36.8 million). Mega settlements (settlements over \$100 million) accounted for 75% percent of all settlement dollars in 2012. See Ellen Ryan & Laura Simmons, CORNERSTONE RES., SECURITIES CLASS ACTION SETTLEMENTS: 2012 REVIEW AND ANALYSIS (2013) (exploring the implications and causes of several class action settlements); see also Renzo Comolli et al., *Recent Trends in Securities Class Action Litigation: 2012 Mid-Year Review: Settlements Bigger, But Fewer*, NERA, July 24, 2012 (describing the rise of recent claims in the past several years).

¹³⁵ Warren, *supra* note 132, at 1080–83 (describing the structure of U.S. class actions and the failure of the regulatory regime).

¹³⁶ *Id.* at 1081–82 (asserting the weaknesses of the securities class action).

¹³⁷ WARD FARNSWORTH, THE LEGAL ANALYST 218 (2007) (describing hindsight bias).

explained without being informed about the outcome (i.e. the accident).¹³⁸ This is simply because, after the incident, it is often hard to imagine that it may not have been foreseeable.¹³⁹ Hindsight bias is said to “blur the distinction between fraud and mistake.”¹⁴⁰ Looking at the securities-fraud cases, scholars found that judges do identify the influence of hindsight on the jury.¹⁴¹ However, a remedy to correct this serious problem is yet to be found, and juries may be punishing fraud and mistake equally.¹⁴²

In stark contrast to these concerns, those who have greater discretion afforded to managers by principles-based standards would significantly weaken a plaintiff's chances to prove a corporate misstatement and scienter and thereby significantly weaken the effectiveness of securities law in general.¹⁴³ From a theoretical perspective, it seems more plausible that a less clearly defined standard will lead to a higher, possibly excessive level of deterrence. The law and economics literature on liability suggests that less predictability in the imposition of liability will increase incentives for risk-averse (or even risk-neutral) individuals to avoid possibly harmful actions.¹⁴⁴ The contrary argument seems to assume that compli-

¹³⁸ *Id.* at 218–23 (describing the phenomena of outcome and hindsight bias and how to cope with them); see, e.g., Kim A. Kamin & Jeffrey J. Rachlinski, *Ex Post ≠ Ex Ante: Determining Liability in Hindsight*, 19 L. & HUM. BEHAV. 89 (1995) (showing how participants in hindsight give higher estimates for the probability of a disaster occurring).

¹³⁹ FARNSWORTH, *supra* note 137, at 220 (describing how once an outcome is experienced, it is hard for an individual to believe it was foreseeable at the time); see Donald Langevoort, *The Epistemology of Corporate-Securities Lawyering: Beliefs, Biases and Organizational Behavior*, 63 BROOK. L. REV. 629 (1997) (discussing prevalent biases in managerial behavior and how it affects corporate attorneys).

¹⁴⁰ Mitu Gulati, Jeffrey Rachlinski & Donald Langevoort, *Fraud by Hindsight*, 98 NW. U. L. REV. 773, 774 (2003) (arguing the hindsight blurs the distinction between one's misconduct and her mistake).

¹⁴¹ *Id.* at 775 (finding that one-third of published opinions in securities class action cases mention concerns with hindsight).

¹⁴² *Id.* at 774; see also Jeffrey Rachlinski, *A Positive Psychological Theory of Judging in Hindsight*, 65 U. CHI. L. REV. 571 (1998) (describing psychological views that people often overstate their view of what occurred during an event in the past).

¹⁴³ See, e.g., Phillips, *supra* note 87, at 608–14 (describing the role of GAAP in securities violations); Newman, *supra* note 7, at 860–61 (using a fictitious dialogue to show the necessity of more rigid standards to avoid a gray area that may create conflict between auditors and clients).

¹⁴⁴ John E. Calfee & Richard Craswell, *Some Effects of Uncertainty on Compliance with Legal Standards*, 70 VA. L. REV. 965, 966 (1984) (asserting that uncertainty in the legal standard can cause those who behave according to the highest possible standards to be held liable due to a gray area which was interpreted in the wrong way); Richard Craswell & John E. Calfee, *Deterrence and Uncertain Legal*

ance with the applicable accounting and auditing standards provides a safe harbor from liability; less clearly defined accounting standards would, thus, increase the discretion of the defendant and not that of the court. U.S. courts have consistently refused to grant such a safe harbor to auditors, and have often largely disregarded GAAP. The U.S. Supreme Court has long recognized that GAAP “are far from . . . a canonical set of rules that will ensure identical accounting treatment of identical transactions. GAAP, rather, tolerate a range of ‘reasonable’ treatments, leaving the choice among alternatives to management.”¹⁴⁵ In the view of the courts, compliance with U.S. GAAP does not necessarily provide users of financial statements with transparent or fairly presented information, and thus protection from litigation. Generally, the courts did not permit a defense of formal *compliance* with accounting standards.¹⁴⁶ In the 1969 case of *U.S. v. Simon*, the defendant auditors had induced the audit client to relegate the explanation of one account receivable (which was especially a vehicle for the CEO to borrow money from the company without shareholders knowing about it) to one footnote. During the trial, eight leaders of the accounting profession testified on their behalf that, with the exception of minor technicalities, the accounting treatment was consistent with the applicable standards; seven of these prominent accountants testified that a more revealing disclosure actually would have been improper under GAAP.¹⁴⁷ Nevertheless, the Court of Appeals for the Second Circuit upheld the trial judge’s decision that compliance with GAAP did not provide a defense, but that the critical test was

Standards, 2 J.L. ECON. & ORG. 279, 280 (1986) (describing how uncertainty in legal rules will increase the likelihood that an individual will not comply and also will not be punished); STEVEN SHAVELL, *ECONOMIC ANALYSIS OF ACCIDENT LAW* 97 (1987) (describing a mathematical formula for negligence); Steven Shavell, *Liability for Accidents*, in 1 HANDBOOK OF LAW & ECON. 139, 159–60 (A. Mitchell Polinsky & Steven Shavell eds., 2007) (suggesting that less certain legal standards will result in a higher level of deterrence).

¹⁴⁵ *Thor Power Tool Co. v. Comm’r of Internal Revenue*, 439 U.S. 522, 544 (1979) (holding constitutional that the Internal Revenue Service could regulate how inventory was recorded); *see also* *Ezra Charitable Trust v. Tyco Intern, Ltd.*, 466 F.3d 1, 12 (1st Cir. 2006) (“GAAP can tolerate a range of reasonable approaches.”).

¹⁴⁶ In its Regulation S-X, the SEC requires auditing financial statements by an independent accountant in accordance with generally accepted auditing standards. 17 C.F.R § 210.1-02(d) (2015).

¹⁴⁷ Fred Kuhar, *The Criminal Liability of Public Accountants: A Study of United States v. Simon*, 46 NOTRE DAME L. REV. 564, 593–94 (1971) (listing the eight witnesses in the case and their accolades).

whether the financial statements as a whole fairly presented the financial situation of the firm. If they did not (as was apparently the case), the question on trial would have to be whether the accountants had been acting in good faith.¹⁴⁸ In light of the courts' lack of deference to GAAP, it appears unlikely that more principles-based accounting standards would have more than a marginal effect on the incidence of litigation.

The experience of foreign issuers with U.S. GAAP until 2007 supports this argument, given that many of them faced the consolidation requirement and had to bear significant compliance costs.¹⁴⁹ These costs did not serve to eliminate the risk of litigation in the United States¹⁵⁰ but, rather, demonstrated the acceptance of the fear of litigation as an inevitable part of "the deal" of being listed in the United States, which also, signaled their good quality. There is no evidence that foreign issuers listed in the United States would consider increased litigation risk to be a disadvantage. In fact, they already reported under IFRS, and by virtue of a U.S. listing, that they and their auditors are already exposed to exactly the same litigation risk of which United States issuers and their auditors are supposedly afraid. Moreover, it is often suggested that foreign issuers often seek a listing in the United States *because* of strong enforcement of securities law, which sends a positive signal to potential investors.¹⁵¹ In other words, litigation risk is high in the United States, and a switch to IFRS will most likely neither lower nor substantially increase such a risk.

Some claim that IFRS simply have not yet evolved to a similar

¹⁴⁸ *United States v. Simon*, 425 F.2d 796, 805 (2d Cir. 1969) (involving conspiracy to commit and mislead with fraudulent corporate financial statements).

¹⁴⁹ U.S. CHAMBER OF COMMERCE, COMMISSION ON THE REGULATION OF U.S. CAPITAL MARKETS IN THE 21ST CENTURY: REPORT AND RECOMMENDATIONS 38 (Mar. 2007) (listing requirements for foreign issuers to conduct securities activities in the United States).

¹⁵⁰ *See, e.g., Woo, supra* note 23, at 130–34 (discussing survey data showing that CEOs preferred litigation in the United Kingdom to the United States).

¹⁵¹ *See, e.g., Yuliya Guseva, Cross-Listings and the New World of International Capital: Another Look at the Efficiency and Extraterritoriality of Securities Law*, 44 *GEO. J. INT'L L.* 411, 413–15 (2013) (examining the effect of U.S. regulation on foreign private investors; Edward Rock, *Securities Regulation as Lobster Trap: A Credible Commitment Theory of Mandatory Disclosure*, 23 *CARDOZO L. REV.* 675, 691–96 (2002) (discussing how disclosure standards impact domestic and foreign corporations decisions to "opt-in" to the U.S. system); René M. Stulz, *Securities Laws, Disclosure, and National Capital Markets in the Age of Financial Globalization*, 47 *J. ACCT. RES.* 349, 366 (2009) (showing some firms choose stronger securities laws than those of the country in which they are located if those rules are strictly enforced).

level as U.S. GAAP and will eventually develop into a rules-based set of standards.¹⁵² In this view, U.S. GAAP were originally principles-based but gradually took their contemporary rules-based shape because of litigation risk. The United States is therefore bound to end up with rules-based accounting standards one way or another. Bratton and Cunningham suggest that IFRS in the United States will, over time, become as rules-based as U.S. GAAP by gradually adopting an increasing number of rules.¹⁵³ In their view, Americans will likely grow disenchanted with IASB. IASB, as a globally oriented standard-setter, will not be responsive to “particular demands emanating from a single national interest group or regulator,” which is why “new domestic politics of accounting standard setting will emerge.”¹⁵⁴ Others argue that U.S. GAAP are “too complex and proscriptive, and result in a system in which entities tend to follow form over substance while violating the underlying spirit of transparency.”¹⁵⁵ They expect that “convergence of U.S. GAAP and IFRS will take the best practices of rules-based and principles-based accounting standards Under such a setting, transparency would be greatly enhanced.”¹⁵⁶

In spite of all of the possible benefits, FASB has still not succeeded in reducing the complexity of its standards more than ten years after Enron.¹⁵⁷ The convergence initiatives, namely, revenue

¹⁵² See SEC Work Plan, *supra* note 4 (referring to comment letters from Air Products and Chemicals, Inc. (“Air Products”), Community Health Systems, Inc. (“Community Health”), JP Morgan Chase (“JP Morgan”), The London Centre for International Corporate Governance Law (“London Ctr Int’l Corp Gov Law”), and Edward Randle).

¹⁵³ Bratton & Cunningham, *supra* note 28, at 1008 (predicting that U.S. IFRS will begin a long process of converting to U.S. GAAP).

¹⁵⁴ *Id.* at 1006–08 (weighing domestic market interest against global market share).

¹⁵⁵ RUTH ANN McEWEN, *TRANSPARENCY IN FINANCIAL REPORTING: A CONCISE COMPARISON OF IFRS & U.S. GAAP* 3 (2009).

¹⁵⁶ *Id.*

¹⁵⁷ See, e.g., Russell G. Golden, Chairman, Fin. Accounting Standards Board, Remarks at the AICPA Conference on Current SEC and PCAOB Developments, at 4–7 (Dec. 10, 2013) (transcript available at http://www.fasb.org/cs/ContentServer?c=Document_C&pagename=FASB%2FDocument_C%2FDocumentPage&cid=1176163675405) (explaining future steps of FASB and how they are working towards their mission to “promote transparency,” “reduce complexity,” and ensure continued progress toward the convergence of international accounting standards); see also *Updates from FASB and the SEC: Standards Setting, Outreach and the Convergence Projects*, CPA J. (July 2013), at 14–19 (describing the legacy and progress of the FASB).

recognition, leases, insurance contracts, and financial instruments have been seen as massive barriers in this endeavor. For instance, for lessor accounting, many argued, "if it ain't broke, don't fix it."¹⁵⁸ Revenue recognition, on the other hand, has seen the most agreement between IASB and FASB leaders. The two boards are expected to publish an almost identical standard on revenue recognition.¹⁵⁹

3. THE INTERNATIONALIZATION OF EUROPEAN ACCOUNTING

While in the United States IFRS are sometimes seen as an expansionist project of a European accounting or corporate governance model, the perception is different in Europe, where the introduction of IAS/IFRS continue to be seen as an expansion of Anglo-Saxon capital market tradition that brought fundamental changes to the various continental accounting styles. Section 3.1 describes the background history of continental European accounting, specifically German and French, before the introduction of IFRS. Section 3.2 discusses the introduction of IFRS in Continental Europe and the resistance it faced, again focusing on Germany and France. Section 3.4 describes the *modus vivendi* that accounting seems to have reached for the time being.

3.1. European Accounting Before IAS/IFRS

3.1.1. The Institutional Framework

The legal framework of accounting within the European (Economic) Community ("EEC") that later morphed into the EU must be understood against the backdrop of harmonization in the company law area in general. With the creation of the common market and the free movement of capital during the 1960s, policymakers

¹⁵⁸ Christopher Westfall, *Convergence 2014: The Tip of the Iceberg*, FIN. EXEC. (Dec 1, 2013) (finding that many people in the United States believe that lessor accounting is not broken).

¹⁵⁹ Hoogervorst, *supra* note 22, at 3 (stating the published "final standard will be almost identical between IFRS and U.S. GAAP").

thought it imperative to harmonize important areas of corporate law in order to facilitate the free movement of capital and the establishment of businesses across borders, foster legal certainty, and to avoid a race to laxity.¹⁶⁰ Accounting came on the EEC's harmonization agenda early, and a requirement for all limited-liability entities to disclose a set of financial statements was introduced as an amendment to First Company Law Directive in 1972.¹⁶¹ The enactment of substantive accounting standards, which had already been on the European Community's agenda, followed with the 1978 enactment of the so-called Fourth Directive or Accounting Directive.¹⁶² The United Kingdom had joined the Community in 1973, alongside Ireland and Denmark, which made an agreement on a number of issues considerably more difficult and which ultimately resulted in a greater need to compromise.¹⁶³ In 1983, the European Community passed the Directive on Consolidated Accounts (known as the Seventh Directive),¹⁶⁴ which supplemented

¹⁶⁰ E.g., Luca Enriques, *Company Law Harmonization Reconsidered: What Role for the EC?*, in *EUROPEAN COMPANY LAW IN ACCELERATED PROGRESS* 59, 61 (Steeff M. Bartman ed., 2006) (describing the prevention of a race to the bottom as the main original goal in light of the incipient debate about a possible "race to the bottom" in the U.S.); Jan Wouters, *European Company Law: Quo Vadis?*, 37 *COMMON MKT. L. REV.* 257, 269 (2000) (explaining the EC Commission's rationale for company law harmonization in the 1960s); see also Claus Luttermann, *Accounting as the Documentary Proof of Good Corporate Governance*, in *GERMAN CORPORATE GOVERNANCE IN INTERNATIONAL AND EUROPEAN CONTEXT* 275, 281 (Jean J. du Plessis et al. eds., 2d ed. 2012) (noting the connection between the EC Treaty's freedoms of establishment and freedom of movement of capital on the one hand and accounting harmonization on the other); Friedrich Kübler, *A Shifting Paradigm in European Company Law*, 11 *COLUM. J. EUR. L.* 219, 220-21 (2005) (providing references from the 1970s that purported that the "race to laxity" in the United States was a major factor influencing harmonization).

¹⁶¹ First Council Directive 68/151/EEC, art. 2(1)(f), 1968 O.J. (L 65) 8, art. 2(1)(f) (introduced by Amendment O.J. L 73/89, March 27, 1972). The directive has recently been re-codified as Directive 2009/101/EC of the European Parliament and of the Council, 2009 O.J. (L 258) 11.

¹⁶² Fourth Council Directive 78/660/EEC, 1978 O.J. (L 222) 11, at intro. [Fourth Directive] (discussing the reasons for enacting the accounting standards). Regarding the relationship between the First and Fourth Directive, see VANESSA EDWARDS, *EC COMPANY LAW* 118 (1999) ("The Fourth Directive has its roots in the discussions leading up to the First Directive. . . .").

¹⁶³ See e.g., EDWARDS, *supra* note 162, at 120-21 (discussing U.K. influence in the 1970's); Lisa Evans & Christopher Nobes, *Some Mysteries Relating to the Prudence Principle in the Fourth Directive and in German and British Law*, 5 *EUR. ACCT. REV.* 361, 363-65 (1996) (discussing changes to the original, German-inspired draft as a result of U.K. influence).

¹⁶⁴ Seventh Council Directive 83/349/EEC, 1983 O.J. (L 193) [hereinafter Seventh Directive].

the Accounting Directive's regime for corporate groups (since the Fourth Directive applied to the accounts of the individual business entity). Only in 2013 were the two directives, which had been amended numerous times, recodified in a single new accounting directive.¹⁶⁵

At first glance, the two directives in combination seemed to set forth a comprehensive regime of accounting standards. The Fourth Directive provided that limited liability entities,¹⁶⁶ irrespective of whether they were publicly traded or not, had to set up and disclose financial statements (consisting of a balance sheet, a profit and loss account, and the notes).¹⁶⁷ More importantly, and maybe more unusually from a U.S. perspective, the Fourth Directive included sections on the presentation of financial statements (i.e. on the format of the balance sheet and the income statement)¹⁶⁸ and a plethora of rules for the recognition of assets and liabilities, expenses, and revenue, as well as rules on valuation.¹⁶⁹ These rules – at least in their original form – are far less case-based than IFRS or U.S. GAAP. For example, Articles 35–38 provide valuation rules for fixed assets in general (i.e. at what value they are to be recognized when they have to be written down), and Articles 39–42 do the same for current assets.¹⁷⁰ IFRS are more strongly case-based and

¹⁶⁵ Directive 2013/34/EU, of the European Parliament and of the Council of 26 June 2013 on the Annual Financial Statements, Consolidated Financial Statements and Related Reports of Certain Types of Undertakings, Amending Directive 2006/43/EC of the European Parliament and of the Council and Repealing Council Directives 78/660/EEC and 83/349/EEC, 2013 O.J. (L 182) 19 (according to its Article 53, the Member States will have to implement the new directive by July 20, 2015).

¹⁶⁶ This includes stock corporations (e.g. the public company in the U.K., the *société anonyme* in France, and the *Aktiengesellschaft* in Germany) and limited liability companies (i.e. the private company in the U.K., the *société à responsabilité limitée* in France, and the *Gesellschaft mit beschränkter Haftung* in Germany). In addition, it applies to partnerships where all unlimited partners are companies of the types just mentioned. Fourth Directive, *supra* note 162, art. 1(1).

¹⁶⁷ *Id.* at introduction (noting that the publication of annual accounts, annual reports, and valuation methods for certain companies of limited liability is of “special importance for the protection of members and third parties.”).

¹⁶⁸ *Id.* arts. 9, 10, 22, 23, 26 (outlining one of two balance sheet layout alternatives, which consists of certain defined assets and liabilities, that can be used by member states in presenting profits and losses).

¹⁶⁹ See generally *id.* arts. 31–42.

¹⁷⁰ *Id.* Articles 42a–42f on the use of fair value for financial assets were only introduced in 2001, when the influence of “Anglo-Saxon” accounting concepts oriented toward the capital market was about to reach its peak, and even then remained largely optional. Directive 2001/65/EC of the European Parliament and

have lengthy standards that apply in specific business contexts, such as research and development, construction contracts, property, plant and equipment, or leases.¹⁷¹

The greatest influence on the directives came from the French and German accounting law in place at that time,¹⁷² although the directives added an additional layer of complexity that required all Member States to recodify their accounting laws.¹⁷³ British accounting tradition also had a considerable influence, leading, for example, to the inclusion of the “true and fair view” standard,¹⁷⁴ originally derived from the Companies Act of 1948.¹⁷⁵ Correspond-

of the Council of 27 September 2001, 2001 O.J. (L 283) 28 (amending the Fourth Directive).

¹⁷¹ See IAS 9 (Research and Development), IAS 11 (Construction Contracts), IAS 16 (Property, Plant and Equipment), IAS 17 (Leases).

¹⁷² EDWARDS, *supra* note 162, at 118–21 (discussing the Elemendorff report of 1966, the first proposal of 1969, and the subsequent effect of the United Kingdom and other new Member States); Brigitte Eierle, *Differential Reporting in Germany – A Historical Analysis*, 15 ACCT., BUS. & BUS. HIST. 279, 290 (2005) (noting strong German influence on the Fourth Directive).

¹⁷³ E.g., Eierle, *supra* note 172, at 289–91 (discussing implementation of the directive in Germany); see Gesetz zur Durchführung der Vierten, Siebenten und Achten Richtlinie des Rates der Europäischen Gemeinschaften zur Koordinierung des Gesellschaftsrechts [Bilanzrichtlinien-Gesetz] [BiRiLiG] [Law to Enact the Fourth, Seventh, and Eighth Guidelines of the Council for the European Community for the Coordination of Corporate Law], Dec. 19, 1985, BGBl. I at 2355 (Ger.) (enacting changes to German commercial law mandated by the European Communities to coordinate corporate law among member states).

¹⁷⁴ Fourth Directive, *supra* note 162, art. 2(3–6).

¹⁷⁵ See Lawrence E. Cunningham, *Semiotics, Hermeneutics, and Cash: An Essay on the True and Fair View*, 28 N.C. J. INT'L L. & COM. REG. 893, 904 (2003) (“[I]n Britain, the goal is producing financial statements giving a ‘true and fair view’ of business condition and results. These concepts . . . were utterly alien to non-Dutch Europe until the ‘true and fair’ view was sanctioned by the Fourth Directive in 1978, driven by the United Kingdom’s recent admission to the European Union.”); see also Dieter Ordelheide, *True and Fair View: A European and a German Perspective*, 2 EUR. ACCT. REV. 81, 82 (1993) (describing how it was “Great Britain, which argued for bringing the true and fair view principle into Art. 2 of the Fourth Directive”); Jonathan Rickford, *Legal Approaches to Restricting Distributions to Shareholders: Balance Sheet Tests and Solvency Tests*, 7 EUR. BUS. ORG. L. REV. 135, 147 (2006) (“At a relatively late stage in the negotiation of the [Fourth] Directive, the Anglo-Irish concept of the overriding principle of the ‘true and fair view’ . . . was added.”). This presumably overarching goal of accounting subsequently caused considerable problems; several Member States, including Germany, Austria, Denmark, Sweden and Finland refused to implement Art. 2(5), according to which the reporting firm must, “in exceptional cases” depart from specific accounting rules where they would be incompatible with a “true and fair view” (the so-called “overriding principle”). David Alexander & Eva Eberhartinger, *The True and Fair View in the European Union*, 18 EUR. ACCT. REV. 571, 572 (2009); David Alexander & Eva Jermakowicz, *A True and Fair View of the Princi-*

ingly, the Seventh Directive included requirements regarding how the companies heading corporate groups needed to represent consolidated financial statements and specific rules on the consolidation process.¹⁷⁶

The Fourth and Seventh Directives were often criticized for having dozens of options, including some leaving the choice to the respective Member State in the national implementation of the directive, and some leaving the choice to the reporting firm.¹⁷⁷ The large number of options, which were often the result of compromises between different accounting traditions, have often been given as a reason why the EU never achieved true accounting harmonization. Member States were able to maintain their traditional accounting cultures, and financial statements never became truly comparable.¹⁷⁸

The directives, however, had to be implemented into the Member States' legal systems as formally enacted laws.¹⁷⁹ The content

ples/Rules Debate, 42 ABACUS 132, 139 (2006) (reporting that Germany, Austria and Sweden refused to implement the overriding principle); Lawrence A. Cunningham, *Semiotics, Hermeneutics, and Cash: An Essay on the True and Fair View*, 28 N.C. J. INT'L L. & COM. REG. 893, 910-11 (2003) (explaining how European countries adopted a range of responses to the "true and fair" mandate, from insisting on strict compliance with rules to permitting the override in defined contexts). Moreover, in continental Europe, particularly Germany, traditional goals of accounting such as prudence were considered to predominate the true and fair view. *E.g.*, Evans & Nobes, *supra* note 163 (discussing discrepancies between different linguistic versions of the directive as a possible reason). The interpretation of the overriding principle in French law has remained rather unclear. *Partie législative Code de Commerce*, art. L 123-14 al. 3 2006 (France); *see* CHRISTIAN DE LAUZAINGHEIN, JEAN-LOUIS NAVARRO & DOMINIQUE NECHELIS, *DROIT COMPTABLE* ¶ 361 (3d ed. 2004) (noting that "after twenty years the notion is still unclear").

¹⁷⁶ Seventh Directive, *supra* note 164, arts. 16-35.

¹⁷⁷ *E.g.*, RICHARD M. BUXBAUM & KLAUS J. HOPT, *LEGAL HARMONIZATION AND THE BUSINESS ENTERPRISE* 235 (1988) (noting the Fourth Directive "leaves no less than forty-one options open to the Member States in addition to thirty-five options left to the business enterprises themselves"); Luca Enriques, *EC Company Law Directives and Regulations: How Trivial Are They?*, 27 U. PA. J. INT'L ECON. L. 1, 26-27 (2006) (stating that the Fourth and Seventh directives, respectively, offer forty-five and fifty-seven opt-in or opt-out provisions).

¹⁷⁸ *E.g.*, Werner F. Ebke, *Accounting, Auditing and Global Capital Markets*, in THEODOR BAUMS ET AL., *CORPORATIONS, CAPITAL MARKETS AND BUSINESS IN THE LAW: LIBER AMICORUM RICHARD M. BUXBAUM* 113, 119-20 (2000) (discussing the consequences of different laws and languages in maintaining different accounting cultures). The 2013 recodification of the EU Accounting Directives did not significantly reduce the number of options. *See, e.g.*, Georg Lanfermann, *EU-Rechnungslegungsrichtlinie: Zum Handlungsbedarf des deutschen Gesetzgebers*, DIE WIRTSCHAFTSPRÜFUNG 849, 849-50 (2013).

¹⁷⁹ *E.g.*, EDWARDS, *supra* note 162, at 119 ("Like France, . . . Germany regarded

of financial statements were, thus, more strongly characterized by formal laws in European countries than they ever were in the United States, where—like in the United Kingdom—the tradition has been private standard setting.¹⁸⁰ For example, while in Germany recommendations and standards set by the German Institute of Chartered Accountants were and are influential, it had no official mandate, and its pronouncements had no binding legal force. Germany, thus, did not have a formally recognized standard-setting body until 1999, and even the one created then has a very limited scope of tasks relating mainly to the use of IFRS in consolidated accounts in the specific German context.¹⁸¹

The situation was somewhat different in France. While the French commercial code included provisions on accounting,¹⁸² a committee was set up under the aegis of the ministry of the economy (and composed of representatives of a large number of interest groups) and had the mandate to amend the General Accounting Plan (*Plan comptable général* or PCG), which effectively provided accounting standards.¹⁸³ These standards were, of course, subor-

accounting regulation as a matter for the statute book rather than for guidelines issued by the accountancy profession, as was the tradition in the United Kingdom”).

¹⁸⁰ See C. W. Nobes, *The Evolution of the Harmonising Provisions of the 1980 and 1981 Companies Acts*, 14 ACCT. & BUS. RES. 43, 52 (1983) (concluding that the Fourth Directive will lead to revolutionary changes in British accounting, “because their inspiration comes from outside the Anglo-Saxon world; the most obvious source being the German *Aktiengesetz* of 1965”).

¹⁸¹ See GESETZ ZUR KONTROLLE UND TRANSPARENZ IM UNTERNEHMENSBEREICH (KonTraG) [Law Governing Supervision and Transparency in Business], Mar. 3, 1998, BGBl I at 786, § 5, no. 24, (adding § 342 to the German Commercial Code, which permits the Ministry of Justice to recognize a private standard setter). For information concerning the activities of the *Deutsches Rechnungslegungs Standards Committee* (the standard setting body), see Christian Leuz & Jens Wüstemann, *The Role of Accounting in the German Financial System*, in *THE GERMAN FINANCIAL SYSTEM* 450, 458–59 (Jan Pieter Krahnen & Reinhard H. Schmidt eds., 2004); Matthias Schmidt, *On the Legitimacy of Accounting Standard Setting by Privately Organised Institutions in Germany and Europe*, 54 SCHMALENBACH BUS. REV. 171, 173 (2002) (discussing German “developments in national and supranational accounting regulation”).

¹⁸² *Partie législative Code de Commerce*, art. L 123–12 to L 123–28, 2006 (France) (describing rules for financial accounting methods and balance sheets).

¹⁸³ See CHRISTOPHER NOBES & ROBERT PARKER, *COMPARATIVE INTERNATIONAL ACCOUNTING* 331 (12th ed. 2012) (providing a timeline of the PCG inception and reform in France); Christian Hoarau, *The Reform of the French Standard-Setting System: Its Peculiarities, Limits and Political Context*, 6 ACCT. IN EUR. 127, 129–32 (2009) (providing “a social and historical perspective on accounting standard-setting in France). Between 1998 and 2009, the National Accounting Council (*Conseil natio-*

dinate to the applicable law and had to be promulgated by the ministry of the economy until 2009.¹⁸⁴ Only after a 2007 reform, these standards were replaced with an independent regulatory agency, which, however, is still subject to considerable government influence.¹⁸⁵

Financial statements had to be set up following the rules of the accounting law included in the respective Commercial Code.¹⁸⁶ The implementation of the directive led to a considerable growth of the body of accounting law.¹⁸⁷ Like the directives, these accounting rules always had a higher level of generality than U.S. GAAP or IAS/IFRS. German accounting law refers to “principles of proper bookkeeping,”¹⁸⁸ which, if taken literally, one might under-

nal de la comptabilité or CNC) and the Accounting Regulation Committee (*Comité de Réglementation Comptable* or CRC) shared the standard-setting role, but their pronouncements had to be approved by the ministry of the economy. CHRISTIAN DE LAUZAINGHEIN, JEAN-LOUIS NAVARRO & DOMINIQUE NECHELIS, *DROIT COMPTABLE* ¶ 24 (3rd ed. 2004).

¹⁸⁴ See Christian Hoarau, *International Accounting Harmonization: American Hegemony or Mutual Recognition with Benchmarks?*, 4 EUR. ACCT. REV. 217, 224 (1995) (discussing state and private-sector influence on accounting standard-setting in France).

¹⁸⁵ A 2007 law creating the Accounting Standards Authority (Autorité des Normes Comptables or ANC) came into force in 2009. Rouba Chantiri-Chaudemanche & Christine Pochet, *La normalisation comptable: l'expert, le politique et la mondialisation*, *Comptabilité, Société, Politique. Mélanges en l'honneur du Professeur Bernard Colasse* 143, 145 (Marc Nikitin & Chrystelle Richard eds., 2012); see Bernard Colasse & Christine Pochet, *De la Genèse du Nouveau Conseil National de la Comptabilité (2007): un case d'Isomorphisme Institutionnel?* 15 *COMPTABILITE CONTROLE AUDIT* 7 (2009), translated in Bernard Colasse & Christine Pochet, *The Genesis of the 2007 Conseil National de la Comptabilité: A Case of Institutional Isomorphism?*, 6 ACCT. EUR. 25, 25 (2009) (arguing that the AMC rather resembles the SEC than FASB); Hoarau, *supra* note 183, at 136-39 (discussing the “reform of the CNC and the Creation of the ANC”).

¹⁸⁶ HANDELSGESETZBUCH [HGB] [COMMERCIAL CODE] Oct. 4, 1897, REICHSGESETZBLATT [RGL.] as amended, §§ 238-342e (Ger.) (codifying that financial statements must be set up following the rules of the accounting law included in the Commercial Code); Loi no. 83-353 du 30 avril 1983 (introducing art. L.123-12 to L.123-28 into the French Commercial Code).

¹⁸⁷ For France, see Hoarau, *supra* note 184, at 224 (stating that there were relatively few legal rules in France before the Accounting Act of 1983, which implemented the directives).

¹⁸⁸ According to HGB § 238(1), “every merchant is obligated to keep books and to show his commercial transactions and to show his net asset position in these according to the principles of proper bookkeeping” (own translation, emphasis added). Specifically for corporations and other limited liability entities, Section 264(2) provides that “the financial statements must provide, in compliance with the principles of proper bookkeeping, a view of the company’s assets, liabilities, financial position and profit and losses” corresponding to the actual circumstances. *Id.*

stand as a reference to professional opinion and good accounting practice to fill gaps. Since the 1950s, these principles have been understood in practice as the set of rules deductively developed from the principles underlying accounting law and codified in it.¹⁸⁹ As Leuz and Wüstemann put it, “accounting principles are considered to be legal rules (‘Rechtsnormen’) and not professional standards (‘Fachnormen’).”¹⁹⁰ Consequently, accounting principles have been shaped by similar forces as other laws where the guidance provided by the general legal rules was insufficient. Besides recommendations of the German Institute of Chartered Accountants and the still relatively new “officially recognized” accounting standards committee¹⁹¹ (whose standards have only been provided with a presumption of compatibility with the principle of proper bookkeeping that was widely considered problematic when it was introduced in 1999),¹⁹² substantive requirements for accounting are, in practice, often determined by judicial decisions. This typically applies to tax law issues, given the high degree of book-tax conformity.¹⁹³ Like in other fields of law, academic and professional writing had a certain influence on the practice of legal interpretation.¹⁹⁴

§ 264(2) (own translation, emphasis added); see Ordelheide, *supra* note 175, at 85 (discussing the relationship between German “principles of proper bookkeeping” and the “true and fair view” principle); Alexander & Eberhartinger, *supra* note 175, at 579 (addressing the question whether the “true and fair view” trumps the principles of proper bookkeeping).

¹⁸⁹ Lisa Evans, *Language, Translation and the Problem of International Accounting Communication*, 17 ACCT. AUD. & ACCOUNTABILITY J. 210, 227–28 (2003) (discussing the historical development of the “deductive methods” since the 1950s); Leuz & Wüstemann, *supra* note 181, at 456–57; David Alexander, *Legal Certainty, European-ness and Realpolitik*, 3 ACCT. IN EUR. 65, 71–72 (2006) (pointing out that the GoB “should be expected to change if the purposes of accounting change”).

¹⁹⁰ Leuz & Wüstemann, *supra* note 181, at 457.

¹⁹¹ Ebke, *supra* note 181 (the accounting standards committee remains limited to standards for accounting consolidation).

¹⁹² HANDELSGESETZBUCH [HGB] [COMMERCIAL CODE], Oct. 4, 1897, REICHSGESETZBLATT [RGBL.] as amended, § 342(2) (Ger.) (codifying presumption of compatibility); see Schmidt, *supra* note 181, at 180 (discussing problems of the presumption raised under German constitutional law).

¹⁹³ See *infra* notes 221–232 and accompanying text (discussing book-tax conformity and its impact on law and procedure).

¹⁹⁴ Generally, German law is analyzed by academics and leading practitioners in academic writing. Specifically through so-called “commentaries,” or treatises, these writings expose a field of law organized by section. E.g., Carl Baudenbacher, *Some Remarks on the Method of Civil Law*, 34 TEX. INT’L L. J. 333, 354–55 (1999) (discussing the impact of legal scholars and judges on civil law in European

Thus, in sharp contrast to the U.S., accounting standards were basically enacted as laws. In both France and Germany, the term “accounting law” (*droit comptable* or *Bilanzrecht*) is often used in reference to the respective legal field. As explained above, that should not be understood to imply that there was no sub-legal standard setting. Nevertheless, accounting was not seen merely as a technical matter best left to the accounting profession, but as an issue of legislation.¹⁹⁵ Given the legal consequences of accounting standards, a legislature abdicating its rulemaking power, as has been the case in the U.S. since the early days of securities law in the 1930s, would have been seen as problematic from a constitutional perspective.¹⁹⁶

3.1.2. Continental European Objectives of Accounting

In the United States, there is no doubt about the objective of financial reporting: financial statements are intended to provide timely, useful, and material information to investors in the capital markets. The disclosure of financial information is required by the Securities Act of 1933 (in the context of the registration statement),¹⁹⁷ and perhaps more importantly, as part of the periodical

countries, including Germany). Regarding the significance of academic writing in civil law systems, see generally Bruce W. Frier, *Interpreting Codes*, 89 MICH. L. REV. 2201, 2205 (1991); MARTIJN W. HESSELINK, THE NEW EUROPEAN LEGAL CULTURE 14–17 (2001). These tend to be more detailed than American legal treatises, with the better ones providing guidance even on issues that have not yet arisen in court by establishing a scholarly interpretation of the law. Baudenbacher, *supra* note 194, at 345–55 (evaluating a legal scholar’s proposed method for civil code interpretation and its impact on German law). For an accounting perspective, see Stuart McLeay, Dieter Ordelheide & Steven Young, *Constituent Lobbying and Its Impact on the Development of Financial Reporting Regulations: Evidence from Germany*, 25 ACCT. ORG. & SOC. 79, 84 (2000) (discussing the formulation of German accounting law and standards); Rolf Uwe Fülber & Malte Klein, *Financial Accounting and Reporting in Germany: A Case Study on German Accounting Tradition and Experiences with the IFRS Adoption* 22–24 (2013), available at <http://ssrn.com/abstract=2200805> (discussing the role of traditional German accounting scholarship).

¹⁹⁵ E.g., RICHARD ET AL., *supra* note 1, at 428 (stressing the influence of legislation in France compared to the U.S.).

¹⁹⁶ Functionally, U.S. GAAP could also be seen as law, since violation of GAAP may lead to civil and criminal penalties. See Cunningham, *supra* note 118, at 292, 323–24 (“Federal securities laws vest the SEC with authority to define generally accepted accounting principles.”).

¹⁹⁷ Schedule A, 17 C.F.R. § 230.610a (2010) (detailing the method and procedure for disclosure of financial information); 15 U.S.C. § 77 (2013) (giving authori-

reporting requirements for publicly traded firms under the Securities Exchange Act of 1934.¹⁹⁸ The administrative competence to pass regulations on accounting – including recognition of balance sheet items and valuation – therefore lies with the SEC, which has passed Regulation S-X¹⁹⁹ and other accounting series releases. However, the SEC has overwhelmingly deferred to private standard-setting and has in fact been explicitly permitted to recognize a standard-setting body that conforms to certain legal requirements since Sarbanes-Oxley.²⁰⁰ In any event, within the framework of U.S. Securities Law, financial reporting has always had only one objective, namely, the provision of information to capital markets.

This stands in contrast to the EU law encapsulated in the original accounting directives, under which not only publicly traded firms, but all limited liability entities have to follow the national implementation of the Fourth Directive's accounting rules and must disclose the information to the public by filing it to the commercial register.²⁰¹ The directives thus implemented a wide-ranging scheme of mandatory disclosure, which was seen as the "price" for limited liability, an idea originating in the U.K.²⁰² that

ty to the SEC to regulate the information or document specified in Schedule A).

¹⁹⁸ Securities Exchange Act of 1934, 15 U.S.C. § 78m (detailing contents and requirements of the reports); 15 U.S.C. § 13(a)-(b) (2012) (discussing the reporting and record keeping requirements).

¹⁹⁹ Regulation S-X, 17 C.F.R. § 210.4-01 (detailing the general rules for accounting forms as required by the SEC).

²⁰⁰ Sarbanes-Oxley Act of 2002, Pub L. No. 107-204, 116 Stat. 745, § 108 (inserting § 19(b) into the Securities Act and permitting the SEC to recognize a standard setting body that complies with certain criteria).

²⁰¹ See First Directive, *supra* note 161, art. 1, 2(f) (listing the types of companies that the directive applies to by Member State); Fourth Directive, *supra* note 162, art. 1 (listing corporate types to which the Directive applies); *id.* art. 47 (requiring disclosure of at least a limited set of financial statements for all firms). To be precise, all stock corporations and private limited companies are required to make these disclosures, as well as partnerships whose only personally liable members are such limited liability entities.

²⁰² See Fourth Directive, *supra* note 162, at intro (suggesting that limited liability companies' "activities frequently extend beyond the frontiers of their national territories and, on the other, they offer no safeguards to third parties beyond the amounts of their net assets"); EDWARDS, *supra* note 162, at 123 n.41 ("The latter rationale has a familiar ring for lawyers in the UK, where it has long been the accepted view that extensive disclosure is the price of limited liability."); Jonathan Rickford, *Fundamentals, Developments and Trends in British Company Law—Some Wider Reflections*, 1 EUR. CO. & FIN. L. REV. 391, 408 (2004) (describing publicity as the main protection for creditors and tracing the U.K. legislative development); see also Wolfgang Schön, *Corporate Disclosure in a Competitive Environment—The Quest for a European Framework on Mandatory Disclosure*, 6 J. CORP. L. STUD. 259,

met considerable resistance on the continent.²⁰³ It also connected accounting to the protection of creditors, who are, for private firms, the primary presumed beneficiaries of accounting and mandatory disclosure.²⁰⁴ Even a recent reform intended to eliminate bureaucratic burdens for very small businesses (“micro-entities”) did not completely eliminate the disclosure requirement.²⁰⁵

264 (2006) (“Evidently, the First Directive (and this approach has been confirmed in the Fourth Directive . . .) dwells upon the hypothesis that ‘disclosure’ has to be regarded as a collateral to ‘limited liability’.”).

²⁰³ See, e.g., EDWARDS, *supra* note 162, at 22–23 (discussing German and French resistance to disclosure of accounting information for small firms during the drafting process for the directives). The resistance was particularly fierce in the German *Mittelstand*. Until at least the early 2000s, reportedly about 30% of French SARLs and around 90% of German GmbHs failed to disclose their accounts. Enriques, *supra* note 177, at 14 (discussing Germany’s failure to comply with the Fourth Council Directive); Armour et al., *supra* note 7, at 125 n.46 (“Studies estimate that 30% of French SARLs and non-listed SAs, and 80–95% of Germany’s GmbHs, do not disclose their financial statements.”). The European Court of Justice repeatedly found that sanctions were not strong enough. Case C-97/96, *Daihatsu Deutschland v. Verband deutscher Daihatsu-Händler*, 1997 E.C.R. I-6843; Case C-191/95, *Commission of the European Communities v. Germany*, 1998 E.C.R. I-5449. The court also had to deal with the question of whether mandatory disclosure was a violation of fundamental rights. Case C-435/02, *Axel Springer AG v. Zeitungsverlag Niederrhein*, 2004 E.C.R. I-8663; see Schön, *supra* note 202, at 260–62 (discussing the *Axel-Springer* case, in which the court considered whether “mandatory disclosure in the above-mentioned cases infringe on the freedom to exercise a trade or profession and the freedom of the press as they have evolved in the jurisprudence of the ECJ.”).

²⁰⁴ See Armour et al., *supra* note 7, at 124–25 (discussing differences in U.S. and foreign financial accounting requirements for closely-held corporations). In practice, however, it is doubtful whether creditors ever avail themselves to inspect financial statements submitted to the company register: sophisticated creditors with the capability of using the financial information contained therein (such as banks) will typically have the bargaining power to ask the company to disclose the information voluntarily. See Luca Enriques & Martin Gelter, *How the Old World Encountered the New One: Regulatory Competition and Cooperation in European Corporate and Bankruptcy Law*, 81 TUL. L. REV. 577, 610 (2007) (“For important creditors, such as banks, information provided by mandatory disclosure under the regime of the directive is of little significance because creditors are usually able to gain access directly through the firm’s managers.”). Moreover, the directives do not say *when* financial information has to be disclosed, which is why deadlines vary widely between Member States. *Id.* (citing a deadline of nine months after the balance sheet date for the U.K. and Austria, seven months for Italy and Spain, and twelve months for Germany).

²⁰⁵ See Directive 2012/6/EU, of the European Parliament and the Council of 14 March 2012, Amending Council Directive 78/660/EEC on the Annual Accounts of Certain Types of Companies as Regards Micro-Entities, 2012 O.J. (L 81) 3, amended art. 1a(2)(e) (exempting entities not meeting two out of three thresholds [balance sheet total of € 350,000, net turnover of € 700,000, ten employees] from the disclosure requirement “provided that the balance sheet information

The accounting rules of the Fourth Directive are also linked with the regulation of legal capital under the Second Directive.²⁰⁶ While this directive has also recently been re-codified (its original version was passed in 1976),²⁰⁷ it provides, among other things, rules on capital contributions and distributions to shareholders of stock corporations. Distributions to shareholders through dividends, repurchase of shares, or otherwise, are only permitted as far as equity exceeds stated capital.²⁰⁸ This does not seem too unusual from an American perspective, given that many U.S. corporate laws still have similar distribution constraints, including in the corporate law of Delaware.²⁰⁹ However, these rules have usually

contained therein is duly filed, in accordance with national law, with at least one competent authority designated by the Member State concerned"). In the new, consolidated Accounting Directive, "Micro entities" thus still have to file an abbreviated balance sheet, but it may be more difficult for outsiders to inspect it. Directive 2013/34/EU, *supra* note 165, art. 36(d). For example, in Germany, "micro entities," instead of filing electronically, will be allowed to deposit a simplified balance sheet with the commercial register, which can be looked up on location and will not be accessible over the internet. Karlheinz Küting & Raphael Eichenlaub, *Verabschiedung des MicroBilG (Kleinstkapitalgesellschaften-Bilanzrechtsänderungsgesetz) – Der vereinfachte Jahresabschluss für Kleinstkapitalgesellschaften* [Passage of the MicroBilG (Law Amending Accounting Laws for Very Small Corporations) – Simplified Annual Financial Statements for Micro-Entities] DEUTSCHES STEUERRECHT 2615, 2618 (2012) (Ger.) (describing passage of a new law allowing ultra-small businesses to make abbreviated filings).

²⁰⁶ Second Council Directive 77/91/EEC, on Coordination of Safeguards Which, for the Protection of the Interests of Members and Others, Are Required by Member States of Companies Within the Meaning of the Second Paragraph of Article 58 of the Treaty, in Respect of the Formation of Public Limited Liability Companies and the Maintenance and Alteration of Their Capital, with a View to Making such Safeguards Equivalent, 1976 O.J. (L 26) 1 [hereinafter Second Directive] (providing legal procedure for the formation and maintenance of limited liability companies' capital).

²⁰⁷ Directive 2012/30/EU, of the European Parliament and of the Council of 25 October 2012 on Coordination of Safeguards Which, for the Protection of the Interests of Members and Others, are Required by Member States of Companies Within the Meaning of the Second Paragraph of Article 54 of the Treaty on the Functioning of the European Union, in Respect of the Formation of Public Limited Liability Companies and the Maintenance and Alteration of Their Capital, with a View to Making such Safeguards Equivalent, 2012 O.J. (L 315) 74, at intro. (providing that the purpose of this Directive is to amend and recast the Second Council Directive 77/91/EEC).

²⁰⁸ Second Directive, *supra* note 206, art. 15(1)(a) (limiting distributions); *id.* art. 19(1)(c) (limiting repurchases).

²⁰⁹ Del. Code Ann. tit. 8, § 170 (West 2013) (providing when "directors of every corporation . . . may declare and pay dividends"). The Revised Model Business Corporations Act (RMBCA) did away with these rules, but many States still have them. See BAYLESS MANNING & JAMES J. HANKS, JR., LEGAL CAPITAL 182–

not been taken very seriously in the U.S., partly because it was not clear under which accounting principles the “surplus” available for distribution was to be computed.²¹⁰ Accounting can therefore be manipulated to generate profits if a distribution is desired.²¹¹ In Europe, however, with the Directives’ comprehensive system of accounting principles in place, the accounting rules of the Fourth Directive were intended to be the basis of profit distribution as well, even if the Second Directive only applies to public companies (stock corporations) and not to private limited liability companies.²¹² Member States typically applied largely the same principles of legal capital to the latter type of firm. Therefore, accounting standards, or more precisely accounting laws, were directly relevant to the amount firms were allowed to distribute, and possibly to the amount shareholders could claim.²¹³ Measuring the proper amount of distributions was therefore a central purpose of accounting²¹⁴ and sometimes even thought to be more important than providing accurate information.²¹⁵

In combination, mandatory disclosure for all firms and the capital maintenance objective underlying accounting rules helped to infuse and solidify a greater degree of creditor protection spirit in-

89 (3d ed. 1990) (discussing the policy and procedural reasons for both adjusted net worth tests); James J. Hanks, Jr., *Legal Capital and the Model Business Corporation Act: An Essay for Bayless Manning*, 74 L. & CONTEMP. PROBS. 211, 214 (2011) (“In Delaware, which to this day still has a modified old-style liabilities-plus-stated-capital statute, the concept of revaluation surplus has been adopted by case law.”).

²¹⁰ The only exception seems to be California, which requires at least publicly traded firms to use GAAP. *Infra* note 367.

²¹¹ ROBERT C. CLARK, CORPORATE LAW 618–23 (1986) (showing how a distributable surplus can be created by writing assets up to fair value and other accounting changes).

²¹² Second Directive, *supra* note 206, art. 1 (specifying the types of companies to which the Directive shall apply).

²¹³ Schmidt, *supra* note 181, at 176 (discussing minimum dividends).

²¹⁴ Leuz & Wüstemann, *supra* note 181, at 459; *see also* Axel Haller, *International Accounting Harmonization: American Hegemony or Mutual Recognition with benchmarks? Comments and Additional Notes from a German Perspective*, 4 EUR. ACCT. REV. 235, 236 (1995) (describing the computation of the distributable income as one of the two major purposes of financial accounting in Germany); Eilís Ferran, *The Place for Creditor Protection on the Agenda for Modernisation of Company Law in the European Union*, 3 EUR. CO. & FIN. L. REV. 178, 200–01 (2006) (stating that U.K. companies have been operating on this basis); *id.* at 208–09 (describing the interplay between the Second and Fourth Directives).

²¹⁵ Schmidt, *supra* note 181, at 176 (describing the secondary importance of this goal).

to accounting standards and how they were usually interpreted: reporting entities were supposed to make sure that they did not show more profits than they had actually made.²¹⁶ Thus, under the system of the Fourth Directive, financial accounts had to conform strictly with the historical cost principle in order to avoid distributions to shareholders based on profits that were not realized.²¹⁷ For the same reason, the definition of “assets” that could be capitalized remained relatively narrow.²¹⁸ On the credit side of the balance

²¹⁶ E.g., Rickford, *supra* note 175, at 146–55 (discussing the influence of the Directives on the balance sheet tests); Wolfgang Schön, *Balance Sheet Tests or Solvency Tests—or Both?*, 7 EUR. BUS. ORG. L. REV. 181, 186–87 (2006) (discussing the role of accounting in limiting the distribution of unrealized gains).

²¹⁷ Leuz & Wüstemann, *supra* note 181, at 459 (giving the example of long-term construction contracts, from which profits could only be realized after completion); Ferran, *supra* note 214, at 209–10 (describing the “prudent” position of the Fourth Directive). Note that article 33 of the Fourth Directive always permitted the Member States to allow some degree of revaluation above historical cost under some circumstances, but at the same time required the creation of a non-distributable revaluation reserve in the balance sheet’s equity section. See *id.* at 209–10 (discussing the requirements of the Second and Fourth Directive); Rickford, *supra* note 175, at 152 (“In Member States which permitted revaluations, the effect of the net assets test would be to reduce the profits available for distribution for public companies suffering such losses whether or not they had a surplus in the revaluation reserve.”). While “replacement valuation” was originally only permitted for “tangible fixed assets with limited useful economic lives and for stocks” (art. 33(1)(a)) and for valuation methods taking inflation into account (art. 33(1)(a)), two directives passed in the early 2000s expanded these possibilities to bring the Fourth Directive more in line with IFRS. Directive 2001/65/EC, of the European Parliament and of the Council of 27 September 2001 Amending Directives 78/660/EEC, 83/349/EEC and 86/635/EEC as Regards the Valuation Rules for the Annual and Consolidated Accounts of Certain Types of Companies as well as of Banks and Other Financial Institutions, 2001 O.J. (L 283) 28, at intro. (“[F]air value directive” introducing art. 42a–42d on the “fair valuation” of financial instruments); Directive 2003/51/EC, of the European Parliament and of the Council of 18 June 2003 Amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC on the Annual and Consolidated Accounts of Certain Types of Companies, Banks and Other Financial Institutions and Insurance Undertakings, 2003 O.J. (L 178) 16 (modernization directive introducing, among other things, art. 33(1)(c) permitting the “fair” valuation of fixed assets). In the case of “fair” valuation of financial instruments, no revaluation reserve is required. See Rickford, *supra* note 175, at 156–57.

²¹⁸ Bernhard Pellens & Thorsten Sellhorn, *Improving Creditor Protection Through IFRS Reporting and Solvency Tests*, in LEGAL CAPITAL IN EUROPE 365, 372 (Marcus Lutter ed., 2006) (comparing the definition of assets under German law and under IFRS); Christian Nowotny, *Taxation, Accounting and Transparency: The Missing Trinity of Corporate Life*, in TAX AND CORPORATE GOVERNANCE 101, 104–05 (Wolfgang Schön ed., 2008) (discussing how “financial accounting . . . forms the basis of the computation of the amount of profits that can be distributed to shareholders”); see also RICHARD ET AL., *supra* note 1, at 260–61, 362 (comparing the French and IASB understanding of assets, the latter being rooted in “neoclassic

sheet, losses had to be recognized as soon as they arose (e.g. through provisions for future losses and contingent liabilities).²¹⁹ Hidden reserves were an element of the creditor protection objective that led to an understanding of accounting law permeated by an asymmetric understanding of the prudence principle, *i.e.* a tendency to show losses earlier than comparable profits.²²⁰

The third big difference compared to the United States lies in the role of accounting for taxation. While the Internal Revenue Code provides that “taxable income shall be computed under the method of accounting on the basis of which the taxpayer regularly computes his income in keeping his books,”²²¹ this provision is understood to refer only to the choice between cash and accrual accounting.²²² The actual degree of book tax-conformity in the United States is actually quite low.²²³ The courts have long recognized

theory”). Where the directive originally permitted the capitalization of cost that could be problematic under a narrowly understood asset definition, it prohibited the distribution of the profits resulting from capitalization. See Fourth Directive, *supra* note 162, art. 34(1)(b) (discussing formation cost); *id.* art. 37(1) (discussing expenses for research and development).

²¹⁹ Leuz & Wüstemann, *supra* note 181, at 459–60 (stating that accounting for liabilities and contingent liabilities can be characterized as more prudent than in the U.S.).

²²⁰ Art. 31(1)(c) of the Fourth Directive provides that

[V]aluation must be made on a prudent basis, and in particular: (aa) only profits made at the balance sheet date may be included, (bb) account must be taken of all liabilities arising in the course of the financial year concerned or of a previous one, even if such liabilities become apparent only between the date of the balance sheet and the date on which it is drawn up, (cc) account must be taken of all depreciation, whether the result of the financial year is a loss or a profit.

Fourth Directive, *supra* note 162, art. 31(1)(c). The prudence principle is asymmetric because profits must already have been “made” at the balance sheet date, whereas liabilities must be taken into account if they “arose” during the balance sheet year. See also Karel van Hulle, *Prudence: A Principle or an Attitude?*, 5 EUR. ACCT. REV. 375, 376 (1996) (explaining that prudence was introduced “with a view to protecting the interests of creditors”); Schön, *supra* note 216, at 196 (2006) (“the ‘asymmetry’ between shareholders and creditors leads to a ‘conservative’ framework of accounting law”); Giovanni E. Colombo, *International Accounting Principles (IAS/IFRS), Share Capital and Net Worth*, 4 EUR. CO. & FIN. L. REV. 553, 555 (2007) (comparing this approach with the IFRS where “[t]he ban on the inclusion of non-realized capital gains – characteristic of traditional historic cost balance sheets – is not considered any more [sic]”).

²²¹ I.R.C. § 446(a) (2013).

²²² See, e.g., 2 MERTENS LAW OF FED. INCOME TAX'N § 12:10.

²²³ Henry J. Lischer & Peter N. Märkl, *Conformity Between Financial Accounting and Tax Accounting in the United States and Germany*, in WPK-MITTEILUNGEN, SPECIAL ISSUE JUNE 1997, at 91, 97–98 (describing “general nonconformity”); Ebke,

that the objectives of taxation and financial reporting are too different to allow a close connection.²²⁴ By contrast, book-tax conformity is much stronger in the majority of European countries.²²⁵ In Germany, according to the legal principle of “authoritativeness” (*Maßgeblichkeitsprinzip*), the financial statements of business entities required to draw up financial statements (including corporations and limited liability companies) according to the Commercial Code also form the basis of taxation.²²⁶ Similarly, in France the tax authorities have traditionally insisted on a “principle of unity” according to which financial statements form the basis also for tax accounting.²²⁷

This means that, for example, an accounting option that has been used in a certain way for purposes of disclosure under the applicable financial accounting principles applies also under tax purposes unless mandatory tax law overrides this particular option.²²⁸ Given the financial incentives set by corporate taxes, the practical consequence has usually been the dominance of tax law; firms use accounting options in order to minimize taxes and there-

supra note 178, at 124 (comparing book-tax conformity in the U.S. and Germany); Wolfgang Schön, *The Odd Couple: A Common Future for Financial and Tax Accounting?*, 58 TAX L. REV. 111, 119–22 (2004) (describing the history of increasing divergence between tax and financial accounting).

²²⁴ E.g., *Thor Power Tool Co. v. Comm’r*, 439 U.S. 522, 531–32 (1979) (finding that a corporation’s method of accounting of inventories in alignment with GAAP did not meet the “clear reflection of income” standard).

²²⁵ Peter Essers & Ronald Russo, *The Precious Relationship Between IAS/IFRS, National Tax Accounting Systems and the CCCTB*, in THE INFLUENCE OF IAS/IFRS ON THE CCCTB, TAX ACCOUNTING, DISCLOSURE AND CORPORATE LAW ACCOUNTING CONCEPTS 29, 33 (Peter Essers et al. eds., 2009) (listing EU Member States by strength of book-tax conformity).

²²⁶ EINKOMMENSTEUERGESETZ [ESTG] [INCOME TAX ACT] Oct. 17, 2008, § 5(1) (Ger.) (requiring “merchants” to use their bookkeeping under the commercial law requirements as the basis of their tax returns); see Nowotny, *supra* note 218, at 105 (noting the German theory that the government could be seen as a “dormant partner”).

²²⁷ A. Frydlender & D. Pham, *Relationships Between Accounting and Taxation in France*, 5 EUR. ACCT. REV. SUPPLEMENT 845, 845–46 (1996) (discussing the reasons for historical ties between accounting and taxation in France).

²²⁸ For a closer look at Germany’s accounting and tax principles, see Dieter Pfaff & Thomas Schröer, *The Relationship Between Financial and Tax Accounting in Germany – The Authoritativeness and Reverse Authoritativeness Principle*, 5 EUR. ACCT. REV. SUPPLEMENT 963, 967–69 (1996) (“[C]ommercial accounting law is authoritative for the tax accounts as long as it is supported by GoB and is not in contradiction of any specific tax rules”); for France, see DE LAUZAINGHEIN ET AL., *supra* note 183, ¶ 29 (discussing the relationship between accounting principles and tax law in France).

fore have a strong interest not to show excessive profits in their financial statements.²²⁹ Taxation depends on the profits shown by an individual reporting entity, and not on the consolidated accounts that also include profits made by subsidiaries.²³⁰ Consequently, it would have been theoretically possible to keep the consolidated accounts, which are of interest in the capital markets, free from the influence of taxation. In practice, however, since in principle the same accounting rules applied to both sets of financial statements (with the addition of consolidation rules applicable only to group accounts), accounting standards for both purposes developed largely uniformly because any legislative change to accounting standards was always also discussed in terms of its tax consequences.²³¹ Furthermore, empirical evidence up to the 1990s showed that firms typically used accounting options in similar ways both in individual and group accounts, thus creating an indirect link between group accounts (which only serve information purposes) and individual accounts (which also serve tax and capital maintenance purposes). Tax dependence of consolidated accounts only decreased in the 2000s with the introduction of IFRS on the consolidated level.²³²

²²⁹ E.g., Pfaff & Schröer, *supra* note 228, at 970-72 (discussing the reverse authoritative effect of tax law). Arguably, directors may even be required to minimize the firm's tax burden under their duty of care, which creates some obvious tension with truthfulness in accounting. Wolfgang Schön, *Tax and Corporate Governance: A Legal Approach*, TAX & CORP. GOVERNANCE 31, 46-47 (Wolfgang Schön ed., 2008) (stating that "the minimization of the corporate tax burden is an integral part of the managers' duty of care."). For France, see Frydlander & Pham, *supra* note 227, at 856 (discussing that many French businesses are engrained in tax oriented policies); see also Reginald Hansen, *Assessing and Tax Accounting Principles in the German Civil and Commercial Code and the Impact on Tax Compliance*, 7 EUR. J. L. & ECON. 15, 34 (1998) ("This being so led to the consequence, that most commercial balance sheets in the FRG are totally deformed, at least compared with what they should normally be expected to show.") (footnote omitted) (citations omitted).

²³⁰ E.g. Ebke, *supra* note 178, at 124 (noting that within Germany a group of affiliated companies is not considered a single taxable person for tax purposes).

²³¹ Moreover, when a firm wanted to use accounting options differently in the individual and consolidated accounts (provided that Member State law allowed it), this divergence had to be explained in the notes. Seventh Directive, *supra* note 164, art. 29. This may have discouraged some firms from tailoring its individual accounts to tax purposes and consolidated accounts to purposes of investors.

²³² Maria Gee et al., *The Influence of Tax on IFRS Consolidated Statements: The Convergence of Germany and the UK*, 7 ACCT. IN EUR. 97, 100-06 (2010) (describing the reduction of "tax pollution" in German consolidated accounts in the 2000s). But see Giovanna Gavana et al., *Evolving Connections Between Tax and Financial Re-*

All in all, these non-disclosure purposes of financial reporting had two consequences relevant to the debate about IFRS. First, the objective of limiting distributions to residual claimants (shareholders and the tax authorities) created incentives for firms to deflate their reported earnings, quite in contrast to the capital-markets driven tendency to inflate earnings that is common in the United States and elsewhere today. Arguably, tax goals in particular distracted from the goal of providing a true and fair view.²³³ Second, the high degree of book-tax conformity strengthened state involvement in financial accounting, given the legal and fiscal consequences of the numbers computed with the applicable accounting standards.²³⁴ In particular, private standard setting would have been considered problematic from a constitutional law perspective because of the tax consequences.²³⁵

3.2. *The Growth of Capital Markets and the Decline of Traditional Accounting During the 1990s*

IFRS only entered the European picture described so far at a relatively late point in time. IASB's predecessor body, the IASC (International Accounting Standards Committee), was founded in 1973 upon the initiative of prominent British accountants, along with the participation of accountants from Australia, Canada, France, Germany, Japan, Mexico, the Netherlands, the United Kingdom, and the United States.²³⁶ While there is no way to prove

porting in Italy, 10 ACCT. IN EUR. 43, 45–48 (2013) (finding that in Italy, where publicly traded firms use IFRS also for entity-level accounts, book-tax conformity has decreased in recent years, while it has increased in firms that still use Italian GAAP).

²³³ DE LAUZAINGHEIN ET AL., *supra* note 183, ¶ 377.

²³⁴ *Id.* (explaining the strong influence of tax law on the standard setting process in France).

²³⁵ Schmidt, *supra* note 181, at 172, 180 (discussing the “specific legitimacy concerns” for accounting standard setting “that derive from the German constitution”).

²³⁶ John Flower, *The Future Shape of Harmonization: The EU Versus the IASC Versus the SEC*, 6 EUR. ACCT. REV. 281, 288 (1997) (stating that “[t]he IASC was set up in 1973 at the initiative of Henry Benson” and accountant representatives from nine countries); Stephen A. Zeff, *The Evolution of the IASC into the IASB, and the Challenges It Faces*, 87 ACCT. REV. 807, 809 (2012) (discussing how the British accountant Benson “led a movement to tackle the issue of diverse accounting practices.”).

the participating individuals' true motivation, it is often believed that it was a reaction to the accounting harmonization ambitions of the European Commission, which were seen as a threat to British accounting tradition in the United Kingdom emanating from the continental European statutory approach.²³⁷ At that point, the IASC—as a private, relatively informally constituted association—had no power whatsoever to set accounting standards and acted primarily as a coordinating and consultative body between its members.²³⁸ While in countries following the Anglo-Saxon model, representatives at the IASC were generally sent by the respective accounting standard setter; in countries with an accounting *law* model, representatives at the IFRS generally had no standard setting power at home.²³⁹ Even though the IASC's membership cut across the fault lines between different accounting cultures, there is consensus that it followed an Anglo-American approach.²⁴⁰ The influence of continental European members with little influence on the national standard setting process remained as limited as the influence of the IAS on these jurisdictions. As one commentator put it, the IASC at that time began to be seen in Europe as a "Trojan horse which conceals the Anglo-American accounting enemy inside a more respectable international façade."²⁴¹ French accounting

²³⁷ Anthony G. Hopwood, *Some Reflections on 'The Harmonization of Accounting Within the EU,'* 3 EUR. ACCT. REV. 241, 243 (1994) (linking the formulation of the IASC to the British "extensive political campaign" mobilized in response to fear of "continental Europe statutory and state control"); see also Flower, *supra* note 236, at 288 ("The British accountancy profession was horrified at the thought of being obliged to accept alien accounting principles consequent on Britain's entry into the European Union."); Zeff, *supra* note 236, at 809-10 (discussing how British accountant Benson's formulation of the IASC may have been for "U.K.-centric reasons.").

²³⁸ E.g., Per Thorell & Geoffrey Whittington, *The Harmonization of Accounting Within the EU,* 3 EUR. ACCT. REV. 215, 223 (1994) (describing the "voluntary nature" of the IASC's standards); Zeff, *supra* note 236, at 810 (members committed to using "their 'best endeavours'" to implement IAS).

²³⁹ Colasse, *supra* note 9, at 32.

²⁴⁰ Flower, *supra* note 236, at 288-89 ("[I]t is abundantly clear that . . . the IASC's standards have reflected the Anglo-American approach to financial reporting and have completely ignored the traditional approach of Continental Europe.").

²⁴¹ *Id.* at 289 (quoting CHRISTOPHER NOBES, A STUDY OF THE INTERNATIONAL ACCOUNTING STANDARDS COMMITTEE 21 (1994)); see also Gordon L. Clark et al., *Emergent Frameworks in Global Finance: Accounting Standards and German Supplementary Pensions,* 77 ECON. GEOGRAPHY 250, 255 (2001) ("For some, the IASC is an extension of FASB because the IASC is an agent of the SEC, which represents U.S. nation-state interests in extending the geographic reach of U.S. capital markets");

scholar Bernard Colasse goes even further by suggesting that the IASC remained true to a “Friedmanian conception of corporate responsibility,” which focuses only on the needs of investors, in contrast to continental European models of corporate governance in which corporations serve broader goals.²⁴²

While the IASC was thus initially a bulwark erected to protect the Anglosphere against an onslaught from a regulatory European accounting model, the tide began to change in the 1990s, during which the Anglo-Saxon accounting tradition began to become attractive for at least some large continental European firms. Capital markets began to grow in Europe, and firms increasingly sought to cross-list in New York or London in order to tap new sources of capital.²⁴³ At the same time, continental European governments became increasingly interested in shoring up their capital markets to attract international investors. In retrospect, scholars identified a convergence in corporate governance practices in that period, most of all during the late 1990s.²⁴⁴ Before accounting law could

Haller, *supra* note 214, at 238 (“[I]nternational harmonization is very much perceived as the introduction of the American accounting model”); Jane Fuller, *The Continent’s Largest Companies Are Gearing Up for Change that Should Reduce the Need to Reconcile Accounts to Different Rules. But the Relevance and Reliability of the Measures is Open to Question*, FIN. TIMES, Nov. 23, 2004, at 17 (“[M]ost of the 7,000 companies concerned do not have securities listed in the US and so are less motivated by convergence. . . . Convergence has heightened fears within Europe that this will lead to the import of prescriptive US standards.”).

²⁴² Colasse, *supra* note 9, at 35. Even without providing a citation, it is clear that Colasse is referring to Milton Friedman. See Milton Friedman, *A Friedman Doctrine: The Social Responsibility of Business Is to Increase its Profits*, N.Y. TIMES, Sept. 13, 1970, at SM17 (discussing how “social responsibility” in business means considering the shareholders and customers).

²⁴³ E.g., Flower, *supra* note 236, at 282–86 (discussing the motivation for European firms to tap international capital markets in the 1990s from a contemporary perspective); Zeff, *supra* note 236, at 817–18 (discussing how “Europe’s largest company” and other corporations began to list in New York).

²⁴⁴ See Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L. J. 439, 443 (2001) (“[A]t the beginning of the twenty-first century we are witnessing rapid convergence on the standard shareholder-oriented model as a normative view of corporate structure and governance.”). For a perspective from the accounting literature, see Yuri Biondi, *What do Shareholders Do? Accounting, Ownership and the Theory of the Firm: Implications for Corporate Governance and Reporting*, 2 ACCT. ECON & L. 1, 3, 18 (2012) (discussing the “accounting perspective of the relationship between shareholding and the inner congeries of the enterprise entity”); Yuan Ding et al., *Towards an Understanding of the Phases of Goodwill Accounting in Four Western Capitalist Countries: From Stakeholder Model to Shareholder Model*, 33 ACCT. ORG. & SOC. 718, 739–46 (2008) (arguing that the accounting treatment of goodwill is connected to the respective orientation of capitalism, and suggesting that there has been a trend from stakeholder to shareholder

follow, some pioneering firms spearheaded the trend by adopting accounting standards from the English-speaking world. In most cases, these standards were initially U.S. GAAP, as in the case of Daimler-Benz's 1993 stock issue in New York, and in some cases U.K. GAAP for firms that sought a listing in London.²⁴⁵ None of these firms had a legal mandate to "internationalize" their accounting systems, which in those days was often a term used for applying U.S. GAAP. Instead, in addition to setting up entity-level and consolidated accounts under their respective national law, these large firms put together an additional set of financial statements or reconciliation statements applying the standards required in the respective capital market where they sought a listing.²⁴⁶ The Daimler-Benz case was a watershed for this development, particularly in Germany, since it allowed a direct comparison between German accounting and the U.S. GAAP. While its consolidated financial statements under the German commercial code showed profits of DM 602m., its financial statements under U.S. GAAP actually showed a loss of DM 1,839m.²⁴⁷ Unsurprisingly, this undermined German confidence in the capability of the traditional accounting law to protect creditors through prudent financial accounting.²⁴⁸ Pressure to internationalize accounting grew, until the German parliament passed a law in 1998 that permitted publicly traded firms to draw up consolidated financial statements under "internationally recognized accounting principles" as long as they were still in accordance with EU accounting directives, instead of applying the rules of the German commercial code.²⁴⁹ Public firms

capitalism reflected in accounting).

²⁴⁵ Zeff, *supra* note 236, at 817 (discussing Daimler-Benz's listing on the New York Stock Exchange and results concerning the U.S. GAAP).

²⁴⁶ Eierle, *supra* note 172, at 291 (describing the differentiating reporting requirements between large and small/medium companies).

²⁴⁷ Interestingly, its equity leapt from 17,584 million DM to 26,281 million DM. Flower, *supra* note 236, at 285.

²⁴⁸ See Eierle, *supra* note 172, at 291 (noting a loss of confidence among international investors).

²⁴⁹ HANDELSGESETZBUCH [HGB] [COMMERCIAL CODE], Oct. 4, 1897, REICHSGESETZBLATT [RGL.] as amended, § 292a, as introduced by the GESETZ ZUR VERBESSERUNG DER WETTBEWERBSFÄHIGKEIT DEUTSCHER KONZERNE AN KAPITALMÄRKTE UND ZUR ERLEICHTERUNG DER AUFNAHME VON GESELLSCHAFTERDARLEHEN [KAPITALAUFNAHMEERLEICHTERUNGSGESETZ] [KAPAEG] [Law on the Improvement of the Competitiveness of German Companies in Capital Markets and the Facilitation of Raising Shareholder Debt] [Capital Raising Facilitation Act], Apr. 20, 1998, BGBL. I at 707 (Ger.) (codifying permission for publicly-traded companies to publish financial statements using "internationally recog-

quickly jumped onto the bandwagon; by 1999, more than half of German publicly traded firms already used either U.S. GAAP or IAS for their consolidated financial statements.²⁵⁰ However, as required by the law, they continued to use the standards of the German commercial code for entity-level financial statements, thus maintaining the previous standard for creditor protection and taxation purposes.²⁵¹ Concurrently, in 1999 Germany created the legal basis for a private standard setter in the form of a not-for-profit organization, which was charged with the task of setting “principles for the implementation of consolidated financial statements.”²⁵²

France first permitted the use of IFRS in consolidated financial statements in 1998.²⁵³ Scholars noted a change in French accounting culture, as financial markets became more important and the function of providing financial information to shareholders began to gain ground.²⁵⁴ Besides a number of reforms that better aligned French accounting with IFRS, the most conspicuous change has been the evolution of the French standard-setter. In the 1990s the CNC still had more than a hundred members, which were sup-

nized” standards provided they are identified as such and “in accordance with” EU law); see Eierle, *supra* note 172, at 291–92 (discussing how German reporting techniques lost credibility among international investors).

²⁵⁰ Holger Daske, *Economic Benefits of Adopting IFRS or US-GAAP – Have the Expected Cost of Equity Capital Really Decreased?*, 33 J. BUS. FIN. & ACCT. 329, 336 (2006) (“By 1999, over 50 percent of the DAX 100 index of German listed firms were reporting according to international standards.”).

²⁵¹ Eierle, *supra* note 172, at 291–92 (describing how Germany implemented new rules which differentiated between listed and nonlisted companies).

²⁵² GESETZ ZUR KONTROLLE UND TRANSPARENZ IM UNTERNEHMENSBEREICH [KonTraG] [Law on Control and Transparency in Business], Apr. 27, 1998 BGBL. I, at 786 (Ger.) (introducing, among others, a § 342 into the commercial code that permits the Ministry of Justice to recognize a private standard setter for purposes of principles of consolidated accounts); see Fülbier & Klein, *supra* note 194, at 19–21 (discussing the role of the German Accounting Standards Board).

²⁵³ Loi no. 98-261 du 6 avril 1998 portant réforme de la réglementation comptable et adaptation du régime de la publicité foncière, J.O. no. 82 du 7 avril 1998, p. 5384, art. 6 al. 1 (adding a new section to article number 357-58 to la loi no. 66-537 du juillet 1966 sur les Sociétés Commerciales, section number 357-8-1) (permitting publicly traded firms to apply “international rules translated into French” instead of national French accounting laws and standards, provided that they also conform to community law); see also Hoarau, *supra* note 183, at 133 (noting that this law allowed firms to choose either IAS or U.S. GAAP).

²⁵⁴ E.g., René Ricol, *Vers une normalisation comptable internationale, condition de la transparence de l’information financière*, in LE JUGE ET LE DROIT DE L’ÉCONOMIE MELANGES EN L’HONNEUR DE PIERRE BEZARD 137, 137 (Marie-Charlotte Piniot, Jean-Pierre Dumas & Paul Le Cannu eds., 2002) (noting that “practice has evolved; the rules must follow”).

posed to represent various interest groups, including labor.²⁵⁵ The 1996 reform reduced the number of members in the CNC to fifty-eight, the emphasis among which shifted from representation of interest groups to “technical” competence, which resulted in an increasing role for representatives of international accounting firms.²⁵⁶ The body’s newest incarnation, the ANC, has a board of a handful of full-time members,²⁵⁷ among which the large accounting firms and large publicly traded corporations dominate.²⁵⁸

Not only Germany, but also Austria, Belgium, France, and Italy passed laws permitting firms to use IAS.²⁵⁹ At that time, the EU Commission had already oriented itself toward IFRS,²⁶⁰ which is why the question of whether laws permitting the use of “internationally recognized financial accounting principles” were compatible with a correct implementation of EU law²⁶¹ was never seriously addressed. Ultimately, the EU solved this untenable situation by

²⁵⁵ Colasse & Pochet, *supra* note 185, at 10–11 (discussing the number of members prior to the 1996 reform); Hoarau, *supra* note 183, at 129, 131 (discussing CNC membership during the late 20th century).

²⁵⁶ Colasse & Pochet, *supra* note 185, at 11–12, 30 (noting the “new mix favored professionals . . . at the expense of Government representatives”); *see also* Hoarau, *supra* note 183, at 133, 136 (noting that the state no longer had the dominant role).

²⁵⁷ Hoarau, *supra* note 183, at 138 (noting the ANC has been “restricted to a Collège of sixteen members”).

²⁵⁸ Colasse & Pochet, *supra* note 185, at 13–14 (noting that, while the leadership of the organization is still appointed by various government bodies, the actual standard-setting committee is dominated by the accounting profession); Hoarau, *supra* note 183, at 139 (noting the influence of large companies and accounting firms).

²⁵⁹ Axel Haller et al., *Financial Accounting Developments in the European Union: Past Events and Future Prospects*, 11 EUR. ACCT. REV. 153, 169 (2002) (“Germany, Austria, France, Italy and Belgium . . . changed their national laws”, allowing companies to “base their financial statements on IAS or US GAAP instead of domestic rules.”). For the French law passed in April 1998, *see* Loi no. 98-261, *supra* note 253. Of course, in all cases, entity-level accounts still had to be drawn up under the respective national law.

²⁶⁰ Haller, *supra* note 259, at 170 (noting that the Commission’s strategy was made clear by the mid-1990s).

²⁶¹ *See, e.g.* Wolfgang Schön, *Gesellschafter-, Gläubiger- und Anlegerschutz im Europäischen Bilanzrecht (Shareholder, Creditor and Investor Protection in European Accounting Law)*, 29 ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT 706, 720–25 (Holger Fleischer et al. eds., 2000) (criticizing a tendency to permit a “dynamic interpretation” of the EU directives, and allowing national legislatures to permit firms to use internationally recognized accounting principles that were “in accordance” [*im Einklang*] but not “in compliance” [*in Übereinstimmung*] with the directives, thus complying only with their broad goals, but not necessarily with the specific provisions of the directives).

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passing the IFRS Regulation in 2002, which explicitly required firms to use IAS (now IFRS) that had been endorsed by a new EU body for their consolidated accounts, thus reducing the sphere of application of the directives.²⁶²

The regulation gives EU and EEA Member States the option to require or permit firms to also use IFRS in their entity-level financial statements and also grants the same option to Member States with respect to the entity-level and consolidated accounts of non-listed corporations.²⁶³ The states used this option in a variety of ways:

Country	Entity-level accounts of listed firms	Consolidated accounts of non-listed firms	Entity-level accounts of non-listed firms
Austria	IFRS not permitted	IFRS optional	IFRS not permitted
Belgium	IFRS not permitted	IFRS optional	IFRS not permitted
Bulgaria	IFRS required	IFRS optional for SMEs, required for all others except entities in liquidation and insolvency	IFRS optional for SMEs; required for all others except entities in liquidation and insolvency
Cyprus	IFRS required	IFRS required	IFRS required
Czech Republic	IFRS required	IFRS optional	IFRS not permitted
Denmark	IFRS optional for listed companies which do prepare consolidated accounts; required for listed companies which	IFRS optional	IFRS optional

²⁶² Regulation (EC) 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the Application of International Accounting Standards, art. 5, 2002 O.J. (L 243) 1, 6; *see also* van der Tas & van der Zanden, *supra* note 80, at 8 (observing that the firms were forced to accept IAS).

²⁶³ Regulation (EC) 1606/2002, *supra* note 262.

	do not prepare consolidated accounts		
Estonia	IFRS required	IFRS optional	IFRS optional
Finland	IFRS optional	IFRS optional for companies audited by certified auditors	IFRS optional for companies audited by certified auditors
France	IFRS not permitted	IFRS optional	IFRS not permitted
Germany	IFRS optional, but additional balance sheet under German law required	IFRS optional; required if filed for listing	IFRS optional, but additional balance sheet under German law required
Greece	IFRS required	IFRS optional for companies audited by certified auditors	IFRS optional for companies audited by certified auditors
Hungary	IFRS optional, but additional balance sheet under Hungarian law required	IFRS optional	IFRS optional, but additional balance sheet under Hungarian law required
Iceland	IFRS optional for the years 2005 and 2006; required from 2007	IFRS optional only for medium-sized and big companies	IFRS optional only for medium-sized and big companies; required for the annual accounts of each subsidiary from 2007 if consolidated groups are permitted to use IAS
Ireland	IFRS optional	IFRS optional	IFRS optional
Italy	IFRS required	IFRS optional except for SMEs	IFRS optional except for SMEs
Latvia	IFRS required	IFRS optional	IFRS not permitted

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Liechtenstein	IFRS optional	IFRS optional	IFRS optional
Lithuania	IFRS required	IFRS optional	IFRS optional
Luxemburg	IFRS optional	IFRS optional	IFRS optional
Malta	IFRS required	IFRS required for larger companies deemed significant in the local economy; optional for all others	IFRS required for larger companies deemed significant in the local economy; optional for all others
Netherlands	IFRS optional	IFRS optional	IFRS optional
Norway	IFRS required for listed companies that do not prepare consolidated accounts starting from 2011; optional for others	IFRS optional	IFRS optional
Poland	IFRS optional	IFRS optional for companies filed for admission to public trading, optional for parent company being subsidiary of parent company preparing consolidated accounts in line with IAS	IFRS optional for companies filed for admission to public trading and for companies whose parent company prepares its consolidated accounts in line with IAS
Portugal	IFRS required if the statutory accounts are the only accounts that they published to the market; otherwise optional	IFRS optional	IFRS optional for companies within the scope of consolidation of an entity who applies IAS/IFRS

Romania	IFRS permitted for purposes of information only	IFRS optional for companies which have obligation to draw up consolidated financial statements	IFRS permitted for purposes of information only.
Slovakia	IFRS permitted, and required for companies of public interest.	IFRS required	IFRS optional for listed companies
Slovenia	IFRS optional	IFRS optional	IFRS optional
Spain	IFRS not permitted	IFRS required for groups in which there is a listed company; optional for all others	IFRS not permitted
Sweden	IFRS not permitted	IFRS optional	IFRS not permitted
UK	IFRS optional	IFRS optional	IFRS optional

Table 1: Implementation of Options Under the IAS Regulation in EU and EEA Countries (2010)²⁶⁴

Table 1 demonstrates that IFRS are not as ubiquitous in Europe as a casual American observer might think. Several important Member States, including Germany and France, continue to adhere to their respective traditional accounting standards for non-listed firms and the entity-level accounts even of listed firms. The reason is that IFRS, being drawn up only for the purpose of providing information for capital markets, are not considered suitable for calculating distributable profits under the legal capital system²⁶⁵ or

²⁶⁴ European Commission, *Implementation of the IAS Regulation (1606/2002) in the EU and EEA* (Jan. 7, 2010), available at http://ec.europa.eu/internal_market/accounting/docs/ias/ias-use-of-options2010_en.pdf (showing the status of the implementation of IAS/IFRS, as well as special rules and exceptions, including those for banks, other credit and financial institutions, investment companies, insurance companies, and charities).

²⁶⁵ *E.g.*, Colombo, *supra* note 220, at 554 (arguing that under IFRS the balance sheet's role is solely to inform investors of the "effective" result of the accounting

computing the basis of corporate tax.²⁶⁶ While EU law now permits Member States to use IFRS by giving firms the option to use IFRS in individual accounts, a number of Member States have not decided to do so.

In Germany, for example, after some adjustments, the law now permits all firms to use IFRS in their entity-level accounts, but they additionally have to draw up financial statements under the traditional rules for purposes of distribution of profits and taxation (and to submit it to the commercial register).²⁶⁷ This rule not only fails to provide firms with any cost savings, it basically does not permit them to do anything that they could not have done without the law, since there was clearly never a prohibition against drawing up IFRS statements in addition to the required ones drawn up under German accounting law. Another option would have been to require reconciliation from IFRS to traditional financial statements. Because of the cost of these two options for firms, Italy opted for a third option, namely to require the creation of restricted reserves to prevent unrealized gains (resulting, for example, from write-ups to fair value) from showing up as distributable profits or reserves in

period," without regard to the issue of profit distribution); Schön, *supra* note 216, at 197 (discussing the implications of using the balance sheet model in IFRS); Giovanni Strampelli, *The IAS/IFRS After the Crisis: Limiting the Impact of Fair Value Accounting on Companies' Capital*, 8 EUR. CO. & FIN. L. REV. 1, 7 (2011) (Ger.) (pointing out that many authors have criticized IFRS as inadequate because they are "incompatible with the 'organisational' function of annual accounts.>").

²⁶⁶ E.g., Eve Chiapello & Karim Medjad, *Une privatisation inédite de la norme: Le cas de la politique comptable européenne*, 49 SOCIOLOGIE DU TRAVAIL 46, 54 (2007) (Fr.) (pointing out that in the Anglo-Saxon countries, other than in France, financial and tax accounting are separate).

²⁶⁷ HANDELSGESETZBUCH [HGB] [COMMERCIAL CODE], § 325(2a) (Ger.) (permitting firms to submit financial statements drawn up under IFRS to the commercial register for purposes of disclosure without eliminating the duty to draw up regular financial statements under the rules of the commercial code). Subsection (2a) was introduced by the Gesetz zur Einführung internationaler Rechnungslegungsstandards und zur Sicherung der Qualität der Abschlussprüfung, (Bilanzrechtsreformgesetz - BilReG) of Dec. 4, 2004, BGBl 2004, I, Nr. 65, at 3166.

See e.g., Eierle, *supra* note 172, at 295-96 (noting that the German legislature regards IAS/IFRS as inappropriate for individual financial statements because individual accounts in Germany have both informational and tax/dividend distribution purposes); Luttermann, *supra* note 160, at 284-85 (noting that German law still requires German companies with limited liability to also provide their annual accounts in accordance with the German Commercial Code); see also HANDELSGESETZBUCH [HGB] [COMMERCIAL CODE], § 315a(3) (Ger.) (permitting unlisted firms to draw up financial statements under IFRS endorsed by the EU). § 315a was also introduced with the BilReg (cited above).

the balance sheet.²⁶⁸ France also does not permit the use of IFRS in entity-level accounts.

The European institutional structure of accounting continues to diverge from that of the United States. Unlike FASB in the United States, IASB has by no means been given a blank check to develop accounting standards for Europe. Both on the national and the EU level, it has sometimes been questioned whether it is permissible for the respective legislature to delegate its core function of law-making to a private body that is neither elected nor politically accountable.²⁶⁹ On the EU level, the IAS Regulation applies the “comitology” technique, under which the Accounting Regulatory Committee (ARC) of the EU level endorses a standard promulgated by the IFRS and recommended by the European Financial Reporting Advisory Group (EFRAG) and the Commission.²⁷⁰ Unless the European Parliament or Council of the European Union opposes a standard within three months, the Commission adopts a regulation enforcing the standard as a regulation of the European Union and publishes the regulation in the official journal, thus binding firms in the Member States.²⁷¹ While critics continue to oc-

²⁶⁸ Colombo, *supra* note 220, at 556 (noting that Italy rejected both the hypothesis of drawing up two accounting period balance sheets and that of asking for a “reconciliation account” in favor of allocating unrealized profits in a restricted reserve); Strampelli, *supra* note 265, at 19–20 (describing the Italian approach, which requires IAS/ISFR financial statements to be changed to figure out capital losses and distributable profits, as “asymmetric” insofar as “it only requires unrealized fair value profits to be neutralized”). *But see* Schön, *supra* note 216, at 198 (pointing out that in this case, “the company will virtually be obliged to draw up a second set of accounts,” thus eliminating any cost savings). Note, however, that the Italian legislator chose to permit the offsetting of revaluation reserves with losses, which may result in the permission of distributions when the firm reentered the profit zone earlier than under “traditional” accounting. Strampelli, *supra* note 265, at 25 (arguing for a solution to the risks posed by the Italian approach that ensures that “only reserves formed by injections of capital or allocation of realized profits” are made available to cover losses).

²⁶⁹ See *infra* note 282 and accompanying text (noting criticisms of IASB for its lack of political legitimacy and accountability to a government).

²⁷⁰ E.g., van der Tas & van der Zanden, *supra* note 80, at 9 (describing the endorsement process).

²⁷¹ Article 6 of the IAS Regulation refers to Council Decision 468/1999 (which applies more generally to the so-called “comitology” procedure). Article 5a(3)(c) of this Council decision sets up the three-month period for the parliament and the council to oppose a proposed standard. Council Decision of 28 June 1999, 1999/468/EC, Laying Down the Procedures for the Exercise of Implementing Powers Conferred on the Commission, 1999 O.J. (L184) 23, 26. The Council Decision has since been repealed by and replaced with Regulation 182/2011. However, article 12 of that regulation states that article 5(a) of the Council Decision re-

asionally voice doubts,²⁷² at least the constitutional conundrum seems to have been resolved. EFRAG has so far taken its task very seriously, and in some cases refused to “rubber-stamp” new standards proposed by the IFRS because they were, in EFRAG’s view, not compatible with the objective of providing a true and fair view to investors.²⁷³

3.3. *Continental Criticism of IFRS*

In the past years, the IFRS and the Anglo-Saxon accounting tradition they stand for have been subject to increasing criticism in Europe. A French textbook (comparing French and IFRS accounting), for example, criticizes IFRS as “dangerous and obsolete.”²⁷⁴ In the authors’ view, IASB “pretends to be neutral and independent from any political pressure,” while fundamental flaws in its approach to fair value accounting have been exposed.²⁷⁵ Some have criticized IASB’s (as well as FASB’s) self-congratulatory use of terms such as “high-quality accounting standards.” The German comparative law scholar Bernhard Grossfeld, for example, argues that this kind of language obscures the fact that there is no single measure of quality, and that accounting policy choices (very much

mains effective. Regulation (EU) No. 182/2011, of the European Parliament and of the Council of 16 February 2011, Laying Down the Rules and General Principles Concerning Mechanisms for Control by Member States of the Commission’s Exercise of Implementing Powers, 2011 O.J. (L 55) 13, 18, art. 12 (EU); see *The Endorsement Process in the EU*, EUR. COMM’N, available at http://ec.europa.eu/internal_market/accounting/docs/ias/endorsement_process.pdf (showing, through a chart, the process through which a regulatory standard is endorsed by the European Union).

²⁷² For an example of how there has been some debate as to whether IFRS 3, which does not require amortization of goodwill, is compatible with the European true and fair view principle, rendering its endorsement a mistake, see Jens Wüstemann & Sonja Kierzek, *True and Fair View Revisited—A Reply to Alexander and Nobes*, 3 ACCT. IN EUR. 91, 100 (2006) (Ger.) (suggesting that IFRS 3 does not result in a true and fair view).

²⁷³ IAS Regulation, art. 3(2) requires that standards “meet the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.” Regulation (EC) 1606/2002 *supra* note 262, at 5–6.

²⁷⁴ RICHARD ET AL., *supra* note 1, at 2.

²⁷⁵ *Id.* at 1; see also Colasse, *supra* note 9, at 35–36 (criticizing that IASB developed a rhetoric of competence, independence, and impartiality to enhance its perceived legitimacy).

like choices of legal policy) inevitably involve value judgments.²⁷⁶

A considerable part of the critique seems to be directed against fair value accounting,²⁷⁷ which is sometimes blamed for exacerbating some effects of the financial crisis: as financial assets are required to be shown at their current market value, they arguably gained value quickly during the period leading up to the financial crisis, thus inflating the amount of assets held by financial institutions, and then fell equally quickly after the bust, thus undermining financial institutions' capital base and pushing them out of compliance with regulatory requirements.²⁷⁸ The critique in the context of accounting is broader. Fair value accounting, as opposed to historical cost accounting, allows profits to be shown that have not yet been realized, which, as discussed above, may allow firms to distribute profits that are not yet certain and may easily be reversed by subsequent losses. This may lead to pressure from shareholders to distribute these (arguably fictional) profits, which, in turn, may lead to a reduction in liquidity, particularly when fair value arguably renders net assets more volatile. Just before the onset of the financial crisis, a German group of accounting professors and professionals christened "Saarbrücken Initiative Against Fair Value" expressed concern that the term fair value is too vague, leaves too much discretion to firms and their auditors, enhances opportunities to manipulate earnings and equity, and thus makes it generally more difficult to analyze financial statements objectively.²⁷⁹ Similarly, French scholars have criticized that IFRS have

²⁷⁶ See, e.g., Bernhard Grossfeld, *Global Accounting: Where Internet Meets Geography*, 48 AM. J. COMP. L. 261, 294-300 (2000) (criticizing FASB's and IASB's use of the term "high quality" accounting standards as "magical words" tantamount to "self-flattery" and intended to put down other accounting systems); Yuri Biondi, *The Pure Logic of Accounting: A Critique of the Fair Value Revolution*, 1 ACCT. ECON. & L. 1, 3, 6, 21, 25 (2011) (comparing the language used by the Anglo-Saxon accounting standard setters to "Newspeak" in George Orwell's 1984).

²⁷⁷ See, e.g., Bernard Raffournier, *Les oppositions françaises à l'adoption des IFRS: examen critique et tentative d'explication*, 13 COMPTIBILITE - CONTROLE - AUDIT 21, 24-25 (2007) (Fr.) (summarizing French criticism of fair value and defending IFRS).

²⁷⁸ See, e.g., Christian Laux & Christian Leuz, *The Crisis of Fair-Value Accounting: Making Sense of the Recent Debate*, 34 ACCT. ORG. & SOC. 826, 831-32 (2009) (discussing problems banks had with fair value accounting during the financial crisis); Bernard Colasse, *La normalisation comptable internationale face à la crise*, 95 REVUE D'ECONOMIE FINANCIERE 387, 389 (2009) (Fr.) (arguing that fair value accounting played a role in the 2008 economic crisis due to the application of IAS 39).

²⁷⁹ Hartmut Bieg, Peter Bofinger, Karlheinz Küting, Heinz Kußmaul, Gerd Waschbusch & Claus-Peter Weber, *Die Saarbrücker Initiative gegen den Fair Value*, 61 DER BETRIEB 2549-52 (2008); see also Burlaud & Colasse, *supra* note 80, at 165 (crit-

deemphasized the principle of prudence in accounting, and thus reduced the protection of creditors compared to the previous national law.²⁸⁰

Others have criticized IASB's lack of accountability and political legitimacy, as well as a perceived absence of a transparent process. Even the European Parliament, while committing to IASB as a standard-setter, has criticized it as lacking "transparency and accountability as a consequence for not being under the control of any democratically elected parliament."²⁸¹ Similarly, French scholars have criticized IASB for its lack of political legitimacy and accountability to a government, given that it grew out of a professional organization dominated by accounting firms.²⁸² Some of the critique in the French literature ties differences between accounting systems to different models of corporate governance: IFRS, based on fair value accounting, are more strongly based on the needs of financial markets because they reflect short-term developments; they are based on the agency theory view of the corporation and the efficient capital markets hypothesis.²⁸³ Thus, in this view IFRS provide a fit for a corporate governance system characterized by small, short-term investors with little to no long-term interaction with the firm.²⁸⁴ Traditional historical cost accounting standards are said to be, by contrast, more relevant for large, long-term

icizing fair value on the grounds that it is based on internal computations in many areas).

²⁸⁰ See Raffournier, *supra* note 277, at 28-29 (summarizing the criticism against IFRS and arguing that IFRS are merely ending an abnormal privilege for creditors).

²⁸¹ European Parliament, Committee on Economic and Monetary Affairs, Report on International Financial Reporting Standards (IFRS) and the Governance of the International Accounting Standards Board (IASB), A6-0032/2008 (Alexander Radwan Report), *quoted in* Luttermann, *supra* note 160, at 283 (quoting from a report and a non-legislative resolution of the European Parliament).

²⁸² Burlaud & Colasse, *supra* note 80, at 155-56; *see also* Raffournier, *supra* note 277, at 30-33 (summarizing the criticism).

²⁸³ Colasse, *supra* note 278, at 392; Céline Michăilescu & Véronique Rougés, *Le reporting financier: Enjeux actuels*, in *COMPTABILITE, SOCIETE, POLITIQUE - MELANGES EN L'HONNEUR DU PROFESSEUR B. COLASSE* 75, 79 (explaining that IFRS predominantly adhere to the theory of corporate responsibility, but have also relied on the agency theory and theory of efficient markets); *see also* RICHARD ET AL., *supra* note 1, at 363 (suggesting that IFRS are based on neoclassical economic theory).

²⁸⁴ Colasse, *supra* note 278, at 392 (suggesting that, following the lead of FASB, IASB adheres to a Friedmannian conception of corporate responsibility, according to which a business is only responsible to its shareholders).

shareholders, creditors, and employees, who are interested in the long-term viability of the firm.²⁸⁵ The IFRS framework indeed professes to privilege the interests of investors, given that they are the residual risk-bearers of the firm; critics have sometimes argued that it is doubtful that financial investors bear greater risks than other actors, e.g., employees.²⁸⁶

Colasse also criticizes the composition of IFRS, whose independence, in his view, "is a myth resulting from the false idea that an organization is independent if its members are."²⁸⁷ He argues that IASB's members, by and large, went through the same cultural experience and education emphasizing the same vision of economics. Moreover, the majority of them are from English-speaking countries, and most of them were socialized in large international accounting firms; hence, a true debate that integrates different views is not possible.²⁸⁸ As to *due process*, he suggests that only users of financial statements with *financial* interests – but not other stakeholders – can make their voices heard at IASB.²⁸⁹

While this criticism originates from a time even before the financial crisis, its advocates certainly tend to argue their view has been vindicated. While IASB has resiliently defended fair value against the post-financial crisis critique, its long-term viability may well depend on the long-term path of European corporate governance systems. If we will indeed see convergence toward shareholder capitalism, IASB is certainly in line with the development. In light of all of this criticism due to the apparent ill-fit with Continental European financial systems, why did the EU even adopt

²⁸⁵ RICHARD ET AL., *supra* note 1, at 691–92 (suggesting that IFRS prioritize the interests of shareholders desiring dividend payments); Michăilescu & Rougés, *supra* note 283, at 92–93 (arguing that IFRS privilege investors, while undermining the relationship with groups interacting with the firm in the long run, such as employees).

²⁸⁶ See, e.g., Burlaud & Colasse, *supra* note 80, at 161 (stating the proposition that investors differ from one another including with respect to the level of risks that they bear).

²⁸⁷ Colasse, *supra* note 278, at 393.

²⁸⁸ Burlaud & Colasse, *supra* note 80, at 159; see Colasse, *supra* note 278, at 394 (describing the similar Anglo-Saxon backgrounds and accounting firm experiences of the IASB's members).

²⁸⁹ Colasse, *supra* note 9, at 36; Burlaud & Colasse, *supra* note 80, at 160 (mentioning states, representatives of employees, financial analysts, the majority of small and medium-sized enterprises, and academics specifically, and noting both that third-world countries are underrepresented and that changes to IAS 1 were introduced in spite of the opposition of most commentators during the process).

IFRS? First, there was clearly a growing dissatisfaction with the limited success of the harmonization process and the EU's inability to adopt national accounting standards that would lead to comparable financial statements. Given that the Member States could not agree on a transnational standard-setting process within the framework of the EU - which would have required further compromise - it was likely easier to adopt the only existing external international standard, namely IAS/IFRS.²⁹⁰ Given the pressures from, and the then-prevailing political enthusiasm for capital markets, the moment for IFRS seemed to have come; arguably, IASC/IASB used financial analysts to create pressure for publicly traded firms to apply to IAS/IFRS.²⁹¹ Second, the important role (even though it is no longer a one-sided dominance) of the large (now Big Four) accounting firms in IASB may have played a role.²⁹² While the Big Four are by no means internally homogenous across borders, complex, international standards whose application requires substantial training favors firms with international networks. The local incarnations of the Big Four may have seen an opportunity to capture a larger slice of the respective national market.

3.4. *The Road Ahead for Europe*

The discussion above has shown that the problems of IFRS in Continental Europe were considerably greater than in the U.S. However, at least for now, the need for a stronger integration of accounting standards into the legal system in light of their consequences for corporate and tax law seems to have been met. Still, the current situation does not seem entirely satisfactory. Firms applying IFRS still often must have a "dual" accounting system, since they are forced to use IFRS by the IAS Regulation and international capital markets on the one hand, and often to use national account-

²⁹⁰ Chiapello & Medjad, *supra* note 266, at 58-59 (stating that it was easier to adopt a transnational accounting standard-setting process instead of agreeing on a particular national one).

²⁹¹ Michăilescu & Rougés, *supra* note 283, at 85.

²⁹² See, e.g., Colasse, *supra* note 278, at 394 (arguing that because the IASB is an Anglo-Saxon organization, it is more prone to the influence of the big auditing firms); Chiapello & Medjad, *supra* note 266, at 49, 57 (noting the influence of the Big Four firms on IASB).

ing laws by their respective national legislatures on the other hand. Having two sets of accounting standards – even within a single country – undermines the core benefit of accounting standards setting: namely, a relatively large degree of comparability of different firms' financial statements. EU accounting harmonization and IFRS in part came about because financial statements were considered to be insufficiently comparable between countries. However, at this point, IFRS have undermined comparability between different groups of firms within countries and possibly also within single corporate groups, namely where consolidated statements are drawn up under IFRS and entity-level statements under national accounting laws.

Europe will have to find a more persuasive solution. Obviously, the IFRS pose certain challenges if the computation of the distributable and taxable amounts of profits is to be retained as a function of financial accounting. With respect to taxation, policy makers may eventually have to decide whether to integrate financial and tax accounting, or whether to separate them completely. Whereas book-tax conformity has a preparation cost advantage for firms, governments are understandably reluctant to delegate the authority to manipulate their corporate tax base to private actors. The EU has been discussing a possible "common consolidated tax base" (without harmonizing rates) for business in recent years. The EU Commission's 2011 proposal seeks to establish autonomous tax accounting rules that "will not interfere with financial accounts."²⁹³ The debate, however, is far from over.²⁹⁴

With respect to legal limitations to the distribution of profits, one possible long-term solution could be the abandonment of the capital-based creditor protection system implemented by the 2nd Directive. While legal capital was never taken quite seriously as a creditor protection mechanism in the United States,²⁹⁵ it also took enormous heat in the European literature and policy debate in the

²⁹³ *Proposal for a Council Directive on a Common Consolidated Tax Base (CCCTB)*, COM (2011) 121 final, at 5 (2011) (proposing a directive harmonizing the corporate tax base in the EU Member States).

²⁹⁴ For a comprehensive analysis, see generally Essers & Russo, *supra* note 225.

²⁹⁵ See, e.g., Marcel Kahan, *Legal Capital Rules and the Structure of Corporate Law: Some Observations on the Differences Between European and U.S. Approaches*, in *CAPITAL MARKETS AND COMPANY LAW* 145-46 (Klaus J. Hopt & Eddy Wymeersch eds., 2003) ("To oversimplify, the U.S. rules are lax, while the European rules impose some meaningful constraints.").

early and mid-2000s.²⁹⁶ Given the heavy criticism, the EU and national governments may eventually abandon the system and replace it with something else, most likely along the lines of the “Solvency Test” proposed in the *Rickford report* and would thus not rest on accounting.²⁹⁷ At the moment, however, the debate seems to be stalled. An abandonment of the legal capital system would at least make the problem of how to reconcile prudent, creditor-oriented accounting with capital-market oriented accounting moot.

Another possibility would be to gradually decouple distributions constraints from financial statements. Where profits under IFRS seem too optimistic from the creditor protection perspective, firms would be required to have revaluation reserves in their equity showing the amount by which they diverge from prudent, creditor-protection oriented accounting.²⁹⁸ Most importantly, firms applying fair value accounting would have to create revaluation reserves for the amount exceeding historical cost (net of depreciation), which would then have to be excluded from distribution to shareholders.²⁹⁹ The recodified Accounting Directive of 2013 is going in this direction when it allows Member States to revalue assets above historical cost: firms choosing revaluation must create revaluation reserves that may only be distributed if they represent gains that have been “actually realized.”³⁰⁰ UK law already limited

²⁹⁶ See generally John Armour, *Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law*, 63 MOD. L. REV. 355 (2000) (suggesting that the EU rules on the maintenance and raising of share capital do not promote efficiency); John Armour, *Legal Capital: An Outdated Concept?*, 7 EUR. BUS. ORG. L. REV. 5 (2006) (arguing that legal capital fails as a means of protecting creditors’ interests); Luca Enriques & Jonathan R. Macey, *Creditors Versus Capital Formation: The Case Against the European Legal Capital Rules*, 86 CORNELL L. REV. 1166 (2001) (arguing that the E.U. should jettison its “inefficient approach” to legal capital rules); Peter O. Mühlbert & Max Birke, *Legal Capital – Is There a Case Against the European Legal Capital Rules?*, 3 EUR. BUS. ORG. L. REV. 695 (2002) (outlining the criticisms of the European legal capital rules and concluding that these are inefficient and offer poor creditor protection).

²⁹⁷ Jonathan Rickford, *Reforming Capital: Report of the Interdisciplinary Group on Capital Maintenance*, 2004 EUR. BUS. L. REV. 919, 967–82. For a defense of the current regime, see, for example, David Kershaw, *Involuntary Creditors and the Case for Accounting-based Distribution Regulation*, 2 J. BUS. L. 140, 140–65 (2009) (arguing that reliance on accounting-based tests to determine when companies may distribute dividends to shareholders protects involuntary creditors by taking these creditors’ claims into account at an earlier stage than a solvency test).

²⁹⁸ See generally *supra* note 217.

²⁹⁹ Pellens & Sellhorn, *supra* note 218, at 377–79.

³⁰⁰ Directive 2013/34/EU, *supra* note 165, at 30–31 (stating the steps required to distribute revaluation reserves).

distributions to “realized” profits in the Companies Act of 1985,³⁰¹ and Italian law now requires it for firms applying IFRS in the individual accounts.³⁰² Nevertheless, it is to some extent questionable whether this approach is practical. Given the speed of developments in business life, legislatures (possibly even on the EU level) would have to closely follow the development of the IFRS and ponder where additional distribution constraints are necessary in order to pursue such a strategy consistently.

Finally, it is not yet completely clear whether IFRS should be expanded to non-listed firms, where creditor protection and book-tax conformity are most relevant. The IFRS has launched a project “IFRS for SMEs,” the basic approach of which is to by and large apply recognition of the IFRS, but with relaxed provisions on disclosure.³⁰³ However, in light of heavy criticism, it is questionable whether the project will ever receive the endorsement of the EU.³⁰⁴

4. LESSONS FOR THE US DEBATE

As we have seen, the changes in accounting culture brought about by IFRS in Continental European countries were much more

³⁰¹ Companies Act, 1985 (UK), §§ 263–64 (this has now been superseded by the Companies Act, 2006 (UK), pt. 21, c. 1, § 830); see Schön, *supra* note 216, at 198 (arguing that the U.K.’s Companies Act, insofar as it requires the distribution of a company’s profits is only as far as they are “realized,” demonstrates that merging financial accounting under IAS/IFRS and other undistributable reserves is “feasible”); Strampelli, *supra* note 265, at 19 (reporting that the Companies Act, 2006 measures distributable profit by accounting for realized profits and losses).

³⁰² Strampelli, *supra* note 265, at 19–20 (discussing Italy’s treatment of distributions and realized profits).

³⁰³ See *IFRS for SMEs*, IFRS.COM, <http://www.ifrs.org/IFRS-for-SMEs/Pages/IFRS-for-SMEs.aspx> (last visited Sept. 26, 2014) (describing IFRS for SMEs Standard, and the steps the IFRS Foundation and IASB have taken to implement the Standard); see also van der Tas & van der Zanden, *supra* note 80, at 21–22 (discussing the “IFRS for SME” program).

³⁰⁴ “IFRS for SMEs” is not endorsed in the EU and there is no plan for such an adoption in a foreseeable future as “IFRS for SMEs” was assessed to be incompatible with the EU Accounting Directive. See European Financial Reporting Advisory Group, *Compatibility Analysis IFRS for SMEs and the Council Directives*, <http://www.efrag.org/Front/p172-4-272/Compatibility-Analysis-IFRS-for-SMEs-and-the-Council-Directives.aspx> (analyzing the ways in which the “IFRS for SMEs” program is incompatible with the current EU Accounting Directives); Memorandum from ICAEW to Françoise Flores, EFRAG Chair (Apr. 19, 2010), available at www.efrag.org (answering specific questions regarding the “IFRS for SMEs” and its compatibility with the EU Accounting Directives).

radical than a shift from GAAP to IFRS would be in the United States, where both GAAP and IFRS are firmly established in Anglo-Saxon accounting culture. There are, however, a number of remaining hurdles and implementation issues, which we address in this section. First, we address the question of whether the U.S. should require firms to use IFRS, or whether it should give them the option of using it. Do we want a monopoly or competition in the setting of financial reporting standards? Section 4.1.1. analyzes the possibility of mandatory adoption of IFRS for U.S. issuers, while section 4.1.2. looks at the possibility of giving an option to U.S. issuers to adopt IFRS if they desire to do so. Second, we look at the possible institutional integration of IASB into the U.S. legal system. Does it matter how IASB is funded? What will the fate of FASB be in this case? Section 4.2.1. seeks alternative setups for FASB. Section 4.2.2. discusses the controversial issue of funding.

4.1. IFRS or U.S. GAAP?

4.1.1. Should U.S. Firms Be Required to Apply IFRS?

As we have seen in section 2.2., the substantive arguments against IFRS per se are rather weak; the criticism relates primarily to their purported principles-orientation, which could also be seen as the strong point of IFRS against the backdrop of accounting scandals. A more rules-based accounting system may, to some extent, be the consequence of the U.S. accounting profession's desire to avoid litigation.³⁰⁵ Given that bright-line rules seem to have encouraged circumvention, IFRS's supposed lack of specification, which arguably makes circumvention more difficult, may well be an advantage. Even if capture by the accounting profession inevitably results in the coalescence of general principles into rules over time,³⁰⁶ it may at least temporarily be beneficial to "reboot" the system and focus on principles.

³⁰⁵ See *supra* notes 94 and 117 with the accompanying text (discussing the choice between a principle based accounting system or one that used bright-lined rules); see also Goldschmid, *supra* note 31, at 5-7 (arguing that the SEC should take steps to incorporate IFRS).

³⁰⁶ Bratton & Cunningham, *supra* note 28, at 1008 (positing that the U.S. IFRS will eventually "revert" back to U.S. GAAP).

The most fundamental argument in favor of IFRS, however, is comparability. In globalizing capital markets, it seems to make little sense for some firms to apply one accounting system while others use another, which will obviously make comparisons by investors and analysts more difficult on the margin. Arguably, if one believes that financial markets should be global, global accounting standards must follow.³⁰⁷

Other objections to IFRS in the U.S., as we have seen, relate to their institutional integration into the U.S. financial system, namely the sheer size of the U.S. economy and problems of delegating a quasi-legislative function to an international body. As to market size, any problems arising from it clearly can only be transitory, as adjustment to IFRS may take time for firms and investors. However, this problem seems to pale in comparison to the Continental Europe's transition to IFRS, which, contrary to popular belief, is far from complete. While it may be difficult to set a new course for a large, inert ship such as the U.S. economy, as we have seen in section 3 the smaller vessels of the Continental European financial systems may break with the past much more radically. In fact, these countries may set a completely new course that diverges much more from their previous traditions than the course of the IFRS diverges from U.S. GAAP, which developed within the same tradition of investor orientation. If comparability is a virtue, then there seems to be no reason to stick to GAAP.

The SEC is unlikely to rush towards mandatory adoption in part because of the ongoing recession. For all the economic, regulatory, and political difficulties,³⁰⁸ the real fear seems to be the high first-time adoption costs, which would excessively burden firms in difficult economic times.³⁰⁹ Many U.S. companies are already con-

³⁰⁷ See *supra* note 28.

³⁰⁸ Hail et al., *supra* note 13 (discussing the many political and regulatory costs that must be taken into account when determining whether or not to adopt the IFRS).

³⁰⁹ See, e.g., Hail et al., *supra* note 44 (detailing the potential costs and benefits of adopting IFRS in the U.S. and concluding that all firms and the entire U.S. economy will bear the "one-time transition costs"); Hans Hoogervorst, Chair, Int'l Acct. Standards Bd., Address at IFRS Foundation/AICPA Conference, Boston (Oct. 5, 2011) ("Many American companies worry about the costs of adopting IFRSs. Let's not beat about the bush; these are real costs"); see also SEC Concept Release, *supra* note 4, at 29-30 (explaining that the transition period will be relatively long and the SEC will provide enough time - four years or so - before mandatory adoption); Mary L. Schapiro, SEC Chairman, Speech by SEC Chairman: Statement at SEC Open Meeting - Global Accounting Standards (Feb. 24, 2010)

cerned about a possible mandatory adoption and have stated that its high costs make such a switch undesirable, at least in the short term.³¹⁰

Again, this argument does not seem entirely persuasive in light of the European experience. True, the EU “switched” to the IFRS in better economic times, namely the mid-2000s, when enthusiasm for capital markets was still running high. However, given the greater distance between the accounting cultures of many European countries from the IFRS, arguably, one would expect the switching cost in the U.S. to be lower. However, an SEC study published in 2008 estimated the switching cost for United States companies to be likely higher than those for comparable European companies, namely between 0.125% to 0.13% of revenue for U.S. issuers compared to 0.05% for EU companies.³¹¹ This translates into a switching cost of \$32 million per U.S. issuer.³¹² Yet these numbers are at the very least questionable. For instance, in Canada, where IFRS have been mandatory since 2011, a survey of 146 companies showed that Canadian companies budgeted less than \$500,000 in Canadian dollars for the changeover.³¹³ The SEC roadmap did not explain how these estimates were calculated, while another study, conducted after the SEC report by academics, provides an estimated switching cost of \$420,000 for small firms and \$3.24 million for large ones, thus corresponding to almost one tenth of the SEC estimates.³¹⁴ Since the publication of the SEC study preceded the actual measurement of switching costs in Canada in 2011, the SEC probably should update, if not completely reassess, its estimate.

(explaining that incorporating the IFRS into the U.S. financial reporting system requires investigation into whether this would serve the interests of U.S. investors and markets); Cunningham, *supra* note 2, at 2–4, 11–14 (underscoring the substantial costs of the transition to IFRS in the U.S. and the uncertainty of investor gains).

³¹⁰ See Black et al., *supra* note 31, at 23 (“Many corporations, such as ExxonMobil and Citigroup, believe the costs of IFRS adoption are too high, potentially higher than any benefit received from the conversion. Other companies, such as Walmart, think that implementing changes to financial accounting during a depressed economic climate does not seem wise.”).

³¹¹ SEC Roadmap, Nov. 14, 2008, *supra* note 4, at 116–17 (citing ICAEW, *supra* note 5, and offering the SEC’s own, higher, projections).

³¹² *Id.* at 130 (“For the companies we estimate to be eligible . . . we estimate the costs for issuers of transitioning to IFRS to sum to approximately \$32 million per company . . .”).

³¹³ Oct. 2012 IFRS Foundation Report, *supra* note 4, at 18.

³¹⁴ Hail et al., *supra* note 44, at 373 (estimating the transition costs for small and large U.S. firms using data from Compustat North America in 2005).

Finally, publicly traded firms in several European countries, notably France and Germany, are effectively required to maintain two parallel accounting systems since these jurisdictions are not ready to abandon traditional accounting for purposes of dividend distributions and taxation. U.S. firms would not have this ongoing additional cost since IFRS would simply replace GAAP.

4.1.2. *Should U.S. Firms Be Permitted to Voluntarily Adopt IFRS?*

One may, however, argue that there is no need to require U.S. issuers to apply IFRS, and that one could, at least for the time being, allow U.S. issues to apply IFRS as an alternative to U.S. GAAP. Since 2007, foreign companies cross-listed in the U.S. do not face a "reconciliation to U.S. GAAP" requirement³¹⁵ as long as they are reporting under IFRS.³¹⁶ This option for foreign companies has led to a discussion on whether the SEC should allow U.S. companies to report under IFRS if they prefer to do so. If mandatory adoption is not politically feasible, voluntary adoption might be the next best alternative. Voluntary adoption is favored, among others, by some multinationals,³¹⁷ the American Institute of Certified Public Ac-

³¹⁵ Acceptance from Foreign Private Issuers of Financial Statements, Release Nos. 33-8818; 34-55998, at 9 (proposed July 2, 2007), available at <http://www.sec.gov/rules/proposed/2007/33-8818.pdf> (describing that the SEC proposed amendments to permit foreign private issuers to prepare financial statements in accordance with IFRS "without reconciliation" to GAAP).

³¹⁶ A "foreign private issuer" as defined in Rule 3b-4 under the Exchange Act that files Form 20-F will be eligible to report under IFRS without having to reconcile with U.S. GAAP. See SEC Release, Dec. 21, 2007, *supra* note 15, at 10 (referring to amendments to Form 20-F to allow foreign private issuers to report under IFRS without reconciliation to U.S. GAAP). Also, foreign issuers based in the EU that are unable to assert compliance with IFRS as issued by IASB only because of the EU "IAS 39 carve-out" were permitted to reconcile those financial statements to IFRS as issued by IASB. *Id.* at 36 (noting that the SEC was providing temporary transitional relief to registrants who had taken advantage of the IAS 39 carve-out under IFRS).

³¹⁷ See, e.g., Hoogervorst, *supra* note 309 (listing a number of firms, including Ford, Archer-Daniels-Midland, the Bank of New York Mellon, Kellogg, Chrysler and United Continental Holdings, that have advocated for the adoption of IFRS in the United States); see Michael Rapoport, *U.S. Firms Clash Over Accounting Rules*, WALL ST. J. (July 6, 2011), <http://online.wsj.com/news/articles/SB10001424052702303982504576428091153200076?KEYWORDS=Rapoport&mg=reno64-wsj> (noting that "[l]arger companies, big accounting firms and top rule makers favor the switch [to IFRS]" including

countants (“AICPA”)³¹⁸ and the Big Four.³¹⁹ While the AICPA sees voluntary adoption as a way of providing equal treatment to U.S. companies and their competitors—namely foreign companies that report under IFRS³²⁰—multinationals tend to see it as a cost-saving opportunity. Many multinationals have non-U.S. subsidiaries reporting under IFRS and seek to avoid a costly conversion to U.S. GAAP for consolidation purposes.³²¹ At least for these firms, the long term cost savings would likely be larger than the initial costs of adoption.

Looking at what Europe experienced in the late 1990s and early 2000s, known as the period of the “end of history for corporate law,”³²² capital markets were popular and European firms saw larger benefits from tapping capital markets that outweighed

Ford Motor Company).

³¹⁸ See Press Release, Am. Inst. of CPAs (“AICPA”), AICPA Recommends SEC Allow Optional Adoption of IFRS by U.S. Public Companies (Aug. 17, 2011) [hereinafter AICPA Recommendations], available at <http://www.aicpa.org/press/pressreleases/2011/pages/aicparecommendssecallowoptionaladoptionofifrsbyuspubliccompanies.aspx> (recommending that the SEC allow U.S. public companies to use IFRS standards while the SEC determines whether to officially adopt such standards, and regardless of whether the IFRS are ultimately adopted).

³¹⁹ See, e.g., *Point of View—The Path Forward for International Standards in the United States: Considering Possible Alternatives*, PRICEWATERHOUSECOOPERS, LLP (Oct. 2011), <http://www.pwc.com/us/en/point-of-view/assets/use-of-ifrs-in-us.pdf> (“[T]he SEC should target the beginning of 2015 to allow U.S. companies to optionally adopt international standards.”).

See also *Accounting Standards in the US—Convergence with IFRS*, FINANCIER WORLDWIDE (Nov. 2011), <http://www.financierworldwide.com/accounting-standards-in-the-us-convergence-with-ifrs> (discussing the merits of allowing companies to voluntarily adopt either GAAP or IFRS); *USA-IFRS Condorsement Explained*, INT’L ACCOUNTING SEMINARS (July 1, 2012), <http://www.iaseminars.com/en/condorsement.html> (noting that if IFRS are good enough for foreign issuers trading in the United States, they should suffice for U.S. companies as well).

³²⁰ See AICPA Recommendations, *supra* note 318 (“An adoption option would provide a level of consistency in the treatment of U.S. companies and foreign private issuers that report under IFRS . . .”).

³²¹ See, e.g., Emily Chasan, *Accountants Give International Rules Short Shift*, CFO Report, WALL ST. J. (Aug. 17, 2011, 12:17 PM) (discussing why AICPA and some U.S.-based multinational companies prefer adoption of the IFRS to be optional instead of mandatory); see also Hoogervorst, *supra* note 309 (noting that “Ford Motor Company sees IFRSs as an important element of its ‘One Ford’ strategy” and pointing out the advantages of standardization in a multinational firm).

³²² See generally Hansmann & Kraakman, *supra* note 244 (arguing that the global acceptance of the shareholder primacy (or “standard”) model will lead to increasing convergence of corporate law).

Daimler-Benz-style revaluations.³²³ Arguably, the Daimler-Benz incident was the catalyst for change in Europe as the European firms had something to gain at the time – namely, accessing the capital markets – but such a change is not going to take place in the United States when there is no evidence of a similar collaborative gain. There is rather a firm-specific gain mostly for the multinationals, whereas for the rest it seems to be more of an overwhelming cost at this point.

Thus, an option for publicly traded U.S. companies to report under IFRS would permit firms to engage a cost-benefit analysis before they switch. The firms themselves are likely better positioned to make an assessment about which standards are superior from a business perspective. However, individual firms will not weigh all social benefits arising from worldwide standardization of accounting standards and increased comparability. Because of these network benefits, financial disclosure is often thought to have a public good component, which is why firms would not produce the socially optimal amount in the absence of regulation.³²⁴ Surveys reveal that few firms are likely to switch immediately to IFRS, even if they are given the option to do so.³²⁵ If this is indeed the

³²³ See *supra* Section 3.2. (“Capital markets began to grow in Europe, and firms increasingly sought to cross-list in New York or London in order to tap new sources of capital”).

³²⁴ See, e.g., Harry I. Wolk, James L. Dodd & John J. Rozycki, ACCOUNTING THEORY: CONCEPTUAL ISSUES IN A POLITICAL AND ECONOMIC ENVIRONMENT 105–07 (8th ed. 2012) (explaining that “overall, . . . there is reason to believe that accounting regulation produces a net benefit to society.”); John C. Coffee, Jr., *Market Failure and the Economic Case for a Mandatory Disclosure System*, 70 VA. L. REV. 717, 723–27 n.23 (1984) (defining a public good as being non-excludable and indivisible and stating that public securities information falls under such a definition); Cunningham, *supra* note 2, at 26–28, 63 (discussing benefits and costs of allowing a market in accounting standards in the United States and noting that “[o]nce information is seen as a public good, the need to generate it to reduce information asymmetries appears.”); Jeffrey N. Gordon & Lewis A. Kornhauser, *Efficient Markets, Costly Information, and Securities Research*, 60 N.Y.U. L. REV. 761, 791–92 n.76 (1985) (using a prisoner’s dilemma scenario to articulate and problematize the information paradox, according to which an investor will be discouraged from gaining market information because no individual can secure gains due to the efficiency of the market); see also *supra* Section 2.2.1., “Too Big to Fail: The U.S. Economy and the Role of the SEC” (explaining how the public good of corporations’ publicly disclosed financial information is a key rationale for making such disclosures mandatory).

³²⁵ See Marie Leone, *Ready but Not Eager for IFRS*, CFO.COM (Nov. 2, 2010), <http://ww2.cfo.com/accounting-tax/2010/11/ready-but-not-eager-for-ifrs> (quoting a survey from August 2010 of accounting and financial reporting executives in relation to IFRS, that finds that most companies believe they could adopt IFRS by

case, allowing the small number of potential first time adopters to switch voluntarily to IFRS might offer exactly the stress test the SEC needs to assess the next steps.³²⁶ The data from voluntary adoption would likely help the SEC to engage in discussions with U.S. issuers whether IFRS should be mandated for all publicly traded companies.

4.1.3. *Should There Be Regulatory Competition Between Standard-Setters?*

A possible choice of two different sets of accounting standards raises the question whether regulatory competition is desirable in this area, or whether one accounting standard setter should have a monopoly, irrespective of the content of accounting standards. There are of course similar debates in many other fields, possibly most prominently – and most closely relevant – in corporate law. To keep it short, proponents of a “race to the bottom” argue that choice between different sets of laws allows firms to select a regime that benefits managers, while shareholders are inadequately protected.³²⁷ Adherents of the “race to the top” school, by contrast,

2016 but were not likely make a switch until SEC requires them to do so); *see also* 2011 US IFRS OUTLOOK SURVEY (2011), PRICEWATERHOUSECOOPERS, LLP, *available at* <http://www.pwc.com/us/en/issues/ifrs-reporting/publications/2011-ifrs-implementation-survey.jhtm> (surveying various industries and companies of various sizes and finding that, if given the option to voluntarily adopt IFRS, only 21% would definitely consider voluntary adoption).

³²⁶ *See* AICPA: *Allow US Companies the IFRS Option Now*, J. ACCT (Oct. 6, 2011), *available at* <http://www.journalofaccountancy.com/Web/20114658.htm> (quoting a 2011 speech from the President and CEO of AICPA in which he called on the SEC to immediately allow U.S. companies to use IFRS); *see also* Hoogervorst, *supra* note 309 (arguing that a “reasonably long transitional period” would be appropriate for the changeover given the cost); *Accounting Standards in the US – Convergence with IFRS*, *supra* note 319 (quoting Barry Jay Epstein’s view that “[i]t makes sense to level the playing field with foreign private issuers that already have been granted the privilege of using IFRS”); David M. Katz, *Investors Defend FASB Role on IFRS*, CFO.COM (July 8, 2011), <http://www.cfo.com/printable/article.cfm/14587240> (quoting a managing director at Morgan Stanley saying he prefers “a gradual adoption of IFRS that hedges against risk of IFRS failure.”)

³²⁷ *See, e.g.*, William Cary, *Federalism and Corporate Law: Reflections upon Delaware*, 83 YALE L.J. 663, 705 (1974) (arguing that jurisdictions should “import lifting standards” instead of entering the “race to the bottom”); Lucian Bebchuk, *Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law*, 105 HARV. L. REV. 1435, 1440 (1992) (“My analysis indicates that . . .

suggest that firms need to attract investment, which creates an incentive for managers to choose a value-maximizing corporate law.³²⁸ Various intermediate views have developed in the context of the United States;³²⁹ the role of Delaware as a quasi-monopolist and its relationship to the federal government has drawn particular

state competition produces a race for the top with respect to some corporate issues but a race for the bottom with respect to others.”); Stulz, *supra* note 151, at 349 (“[C]ost advantages for a firm’s securities to trade publicly in the country in which that firm is located and for that country to have a market for publicly traded securities distinct from the capital markets of other countries will progressively disappear”); see also Lucian Bebchuk et al., *Does the Evidence Favor State Competition in Corporate Law?*, 90 CALIF. L. REV. 1775, 1820 (2002) (“[T]he body of empirical evidence on which supporters of state competition rely does not warrant their claims of empirical support”); Guhan Subramanian, *The Influence of Antitakeover Statutes on Incorporation Choice: Evidence on the “Race” Debate and Antitakeover Overreaching*, 150 U. PA. L. REV. 1795, 1872 (2002) (summarizing evidence of a race to the bottom, and concluding that managers migrate to states with antitakeover laws).

³²⁸ Ralph Winter, *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEG. STUD. 251, 251–52 & 289–92 (1977) (arguing that the race to the bottom theory is incorrect and that, rather, competition between states creates a race to the top fueled by the desires of managers to value maximize when given a share of residual profits); see ROBERTA ROMANO, *THE GENIUS OF AMERICAN CORPORATE LAW* 14–24 (1993) (arguing that state competition in corporate law does not lead to a race to the bottom but a race to the top); Robert Daines, *Does Delaware Law Improve Firm Value?*, 62 J. FIN. ECON. 525, 533 (2001) (noting that corporations incorporated in Delaware have been worth meaningfully more than firms incorporated elsewhere since at least the early 1980s); Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359, 2427–28 (1998) (suggesting that allowing states to compete in terms of their securities regulations is beneficial for shareholders); Roberta Romano, *Is Regulatory Competition a Problem or Irrelevant for Corporate Governance?*, 21 OXFORD REV. ECON. POL’Y 212, 229 (2005) (“If anything, it is the competition of states in producing corporate law that has, however modestly, facilitated the reorganization of the U.S. economy in the last several decades”); Ralph Winter, *The “Race for the Top” Revisited: A Comment on Eisenberg*, 89 COLUM. L. REV. 1526, 1529 (1989) (suggesting that the race to the top is happening slowly due to the lack of a state competing directly with Delaware).

³²⁹ See, e.g., Ray Ball, *Market and Political/Regulatory Perspectives on the Recent Accounting Scandals*, 47 J. ACCT RESEARCH 277, 317 (2009) (concluding that the U.S. financial market is not as efficient as it has historically been and is unable to prevent violations even though it is able to punish violators); William W. Bratton, *Corporate Law’s Race to Nowhere in Particular*, 44 U. TORONTO L.J. 401, 419 (1994) (noting that the “form and intensity” of the United States’ stance towards corporate law “varies from period to period”); Melvin Eisenberg, *The Structure of Corporation Law*, 89 COLUM. L. REV. 1461, 1512 (1989) (arguing that the U.S. federal government has an incentive to mitigate suboptimal rules but, because the costs of doing so are high, the risk of federal intervention increases if prevailing state law becomes highly suboptimal).

attention.³³⁰ And in the European context, scholars have argued that different ownership structures might lead to different outcomes in regulatory competition.³³¹ Generally, views on where regulatory competition actually leads on the top-bottom continuum depend on what one believes about how well markets work: The more efficient they are, the more likely there is a movement to the top; the more they are distorted by information asymmetries, irrational behavior and cognitive distortions on the part of investors, the more likely managers may be able to exploit these disadvantages.

The debate in the accounting literature parallels the one in corporate law. The two competing views are either to “let the market forces determine how much and what kind of information firms should produce” or “to turn to regulation to protect investors, on the grounds that information is such a complex and important commodity that market forces alone would fail.”³³²

The second view is based on the premise that market forces are not well-suited to incentivize firms to produce the optimal amount of information, given that managers and investors have diverging interests and will eventually try to capture standard-setting processes to pursue them,³³³ and that information asymmetry that in-

³³⁰ See e.g., Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588, 590, 644-46 (2004) (arguing that the chief pressure on Delaware's corporate law comes from the U.S. federal government, which sometimes tolerates and other times intervenes with Delaware law); Mark J. Roe, *Delaware and Washington As Corporate Lawmakers*, 34 DEL. J. CORP. L. 1, 32-33 (2009) (“There is a vast federal presence in the law governing the American corporation and that federal presence affects state-based jurisdictional competition.”).

³³¹ See Hanne Søndergaard Birkmose, *A 'Race to the Bottom' in the EU?* 13 MAASTRICHT J. EUR. & COMP. L. 35, 51-52 (2006); Luca Enriques & Matteo Gatti, *The Uneasy Case for Top-Down Corporate Law Harmonization in the European Union*, 27 U. PA. J. INT'L ECON. L. 939, 950 (2006); Martin Gelter, *The Structure of Regulatory Competition in European Corporate Law*, 5 J. CORP. L. STUD. 247, 273-75 (2005); Federico M. Mucciarelli, *The Function of Corporate Law and the Effects of Reincorporations in the U.S. and the EU*, 20 TUL. J. INT'L & COMP. L. 421, 445 (2012); Tobias H. Tröger, *Choice of Jurisdiction in European Company Law – Perspectives of European Corporate Governance*, 6 EUR. BUS. ORG. L. REV. 3, 28-29 (2005) (all discussing the possibility that reincorporations will be driven by large shareholders rather than management in concentrated ownership systems).

³³² WILLIAM R. SCOTT, FINANCIAL ACCOUNTING THEORY 15 (5th ed. 2009).

³³³ *Id.* at 466; see, e.g., William U. Parfet, *Accounting Subjectivity and Earnings Management: A Preparer Perspective*, 14 ACCT. HORIZONS 481, 484 (2000) (noting that business executives, like all people, are self-interested, and that accounting standards are helpful, although not sufficient, to guard against potential abuse in relation to financial reporting).

vestors face while trading in the market will result in an adverse selection problem.³³⁴ Whether the existence of multiple standard-setters is a vice or a virtue is thus a matter of perspective: proponents of uniform regulation argue that letting standard-setters compete would force each of them to lower its standards as to attract firms and their managers away from the other, thus resulting in a race to bottom.³³⁵

Both in the markets for corporate law and accounting standards, network externalities may play a role:³³⁶ Delaware, by virtue of its developed law and its specialized courts, creates an advantage for firms to incorporate there that is independent from which group its corporate law actually favors. Managers and shareholders, whose interests seem to play the greatest role in the debate, therefore have an additional advantage when choosing Delaware over other states.

In accounting, investors' ability to compare creates a different kind of network externality, which is why mandatory and harmonized disclosure requirements may be necessary to induce firms to produce the desirable amount of information. An individual firm may actually lose because comparability might shed an unfavorable light on it, but, on the aggregate, capital market participants will gain. As financial accounting information is a public good (since it can be shared with those who did not "pay for it"), it arguably will be underproduced under purely voluntary market conditions.³³⁷ In some cases, particularly when a firm issues capi-

³³⁴ E.g., Christian Leuz & Peter Wysocki, *Economic Consequences of Financial Reporting and Disclosure Regulation: A Review and Suggestions for Future Research* 6 (UNIV. OF CHI. & MIT SLOAN SCH. OF MGMT., Working Paper No. 1, 2008) (discussing, among other points, the theory that "information asymmetries among investors introduce adverse selection into share markets . . .").

³³⁵ See, e.g., Ronald Dye & Shyam Sunder, *Why Not Allow FASB and IASB Standards to Compete in the U.S.?*, 15 ACCT. HORIZONS 257, 257 (2001) (considering arguments for and against "introducing competition into the accounting standard-setting process in the U.S. by allowing individual corporations to issue financial reports prepared in accordance with either FASB or ISAB rules"); Karmel & Kelly, *supra* note 24, at 950-51 (arguing that "regulatory competition will lead to a race to the bottom and the absence of meaningful standards" unless "soft law standards" are introduced).

³³⁶ See generally Ramanna & Sletten, *supra* note 46 (highlighting the networking effects that countries have experienced as a result of their adoption of IFRS).

³³⁷ See generally *supra* note 45 and *supra* note 324; Christian Leuz, *Different Approaches to Corporate Reporting Regulation: How Jurisdictions Differ and Why*, 40 ACCT. & BUS. RES. 229, 231 (2010) [hereinafter Leuz, *Corporate Reporting*] (outlining arguments for regulating corporate reporting). But see Leuz & Wysocki, *supra*

tal, firms may be inclined to overproduce information in order to attract investment; however, this incentive typically does not persist after an IPO, thus resulting in an underproduction of information.³³⁸ It is therefore often argued that in a purely market-based system, where firms freely decide on the extent of disclosure (when there is no regulation), firms would not disclose the right level of information.³³⁹ A regulatory solution, as opposed to one where firms privately choose the level of disclosure, may achieve better outcomes and be cheaper, which may be why it is today widespread around the world.³⁴⁰ Regulation, among other advantages, makes it easier to process the information and compare across firms while eliminating the cost of negotiating disclosures with various parties such as shareholders and creditors.³⁴¹

One could therefore argue, with some justification, that the very idea of allowing two sets of accounting standards to compete is incompatible with accounting standard-setting as such.³⁴² If there are multiple standard-setters, comparability between the financial statements of firms using different standards would likely suffer.³⁴³ Advocates of competition suggest that the latter is neces-

note 334, at 16–20 (reviewing arguments for regulating corporate reporting).

³³⁸ Leuz & Wysocki, *supra* note 335, at 17 (“It is easy to imagine situations after the IPO in which firms have incentives to withhold or manipulate information (e.g., when performance is poor.)”).

³³⁹ Leuz, *Corporate Reporting*, *supra* note 338, at 231–32 (discussing the benefits and costs of a regulatory scheme for a company’s financial reporting, and warning that a “solid case for regulation” rather than a market solution is necessary).

³⁴⁰ *Id.* at 232 (“Overall, there seems to be a reasonable case for a mandatory reporting regime. Consistent with this view, mandatory reporting regimes are widespread around the world.”).

³⁴¹ *Id.* at 231 (highlighting various benefits of having a regulatory scheme imposed on a company’s financial reporting and referred to such a scheme as a “low-cost standardised solution”).

³⁴² Cunningham, *supra* note 2, at 4 (arguing that the competing accounting standards framework may pose practical problems and produce negative consequences); Pöschke, *supra* note 28, at 64 (critiquing the aim of comparability).

³⁴³ Cunningham, *supra* note 2, at 4 (“[C]ompetition among accounting standards is inconsistent with comparability in financial reporting.”); Pöschke, *supra* note 28, at 64 (“Any form of option would thwart comparability by allowing for the co-existence of and competition between substantially different accounting systems . . .”). *But see* Hans B. Christensen, Luzi Hail & Christian Leuz, *Mandatory IFRS Reporting and Changes in Enforcement*, 56 J. ACCT. & ECON. 147, 147 (2013) (reporting findings of their study, including that a change in reporting standards does not have an effect on market liquidity).

sary for the evolution of accounting standards, while a monopoly of one standard-setter would eliminate the possibility of comparing alternative methods in the pursuit of identifying the best ones.³⁴⁴ In this view, competition would lead to a race-to-the-top by pushing standard-setters toward the direction of passing better standards and be selected by firms. In fact, a recent study found that “allowing choice between competing standards increases market value over a single uniform standard.”³⁴⁵

Allowing GAAP and IFRS to compete in the U.S. capital market would therefore require at least two conditions to work. First, in-

³⁴⁴ See e.g., SCOTT, *supra* note 333, at 503 (“[C]omplete integration of accounting standards will take some time if, indeed, it is desirable at all. In the meantime, some ability of firms to choose between competing sets of accounting standards should not be ruled out”); Jeremy Bertomeu & Edwige Cheynel, *Toward a Positive Theory of Disclosure Regulation: In Search of Institutional Foundations*, 88 ACCT. REV. 789, 792–93 (2013) (arguing that “[c]ompetition also disciplines standard-setters to cater to different groups and thus encourages the revelation of information through standard adoptions”); Shyam Sunder, *Adverse Effects of Uniform Written Reporting Standards on Accounting Practice, Education, and Research*, 29 J. ACCT. PUB. POL’Y 99, 100 (2010) (“Uniformity discourages research and debate in academic and practice forums, and promotes increasingly detailed rule-making. It shuts the door on learning through experimentation, making it difficult to discover better ways of financial reporting through practice and comparison of alternatives. Improved financial reporting calls for a careful balance between written standards and unwritten social norms.”); Shyam Sunder, *IFRS and the Accounting Consensus*, 23 ACCT. HORIZONS 101, 101, 105–06, 109 (2009) (arguing that a monopoly of IFRS will “discourage discovery of . . . better methods of financial reporting [and] make it difficult [if not impossible] to conduct comparative studies of the consequences of using alternative methods of accounting”); Shyam Sunder, *Regulatory Competition Among Accounting Standards Within and Across International Boundaries*, 21 J. ACCT & PUB. POL’Y 219, 219 (2002) (examining the consequences of regulatory competition on the “quality and efficiency of standards, quality of information provided to shareholders and other interested parties, and the efficiency of corporate governance and managerial actions”); Shyam Sunder, *Uniform Financial Reporting Standards: Reconsidering the Top-Down Push*, 77 CPA J., Apr. 2007, at 6 (2007) (suggesting that there are several advantages of a system of supervised competition among multiple sets of financial reporting standards that allow investors, companies, and auditors to choose from a set of competing standards); see S.P. Kothari, Karthik Ramanna, Douglas J. Skinner, *Implications for GAAP from an Analysis of Positive Research in Accounting*, 50 J. ACCT. & ECON. 246 (2010) (arguing that “competition between the FASB and the IASB would allow GAAP to better respond to market forces”); Roberta Romano, *The Need for Competition in International Securities Regulation*, 2 THEORETICAL INQUIRIES L. 387, 391–92 (2001) (arguing that international securities regulation restricts firms to “only a limited choice of regime” and that these restrictions should be removed “[t]o create a truly competitive regime of securities regulation.”).

³⁴⁵ Bertomeu & Cheynel, *supra* note 344, at 789, 792–93 (outlining the benefits of allowing individual issuers to choose between competing sets of accounting standards).

vestors must be able to assess which accounting standards provide them with the better information. Second, overall market conditions must not make it impossible for two sets of standards to compete on fair terms. Among other things, this means that the choice of accounting standards should not be inherently linked to other institutional factors so that competition on quality is impossible. For example, as discussed above in section 3.2. in the 1990s European firms began to use not only IAS, but also U.S. GAAP in addition to domestic accounting laws and standards.³⁴⁶ At that time, firms seeking a listing at European exchanges generally chose IAS, while those traded in New York had to comply with U.S. GAAP.³⁴⁷ Clearly, the strategic choice of a capital market determined the choice more than the quality of accounting standards. Moreover, since comparability is so essential to financial accounting, there would have to be a significant number of firms for each set of standards to achieve a critical mass. With FASB starting as the market-dominant standard-setter, this would clearly not be a problem for GAAP. U.S. firms switching to IFRS would have a comparative frame primarily in the form of foreign firms, which differ from their U.S. competitors in a variety of other ways and may thus not provide the best comparison.

However, arguably, for over a decade the IFRS and U.S. GAAP convergence process has brought those two sets of standards so close to each other that there is no competition on the merits anyway, and thus comparison between firms applying either standard is not excessively difficult. Competition between two standard-setters would therefore primarily only be about which of the two entities sets the agenda in accounting, and which one follows. Yet, the study on the advantages of competition mentioned above also suggests that these benefits could disappear if competing standard-setters effectively begin to collude by substantively setting the same standards (as FASB and IASB have been doing in their con-

³⁴⁶ See Michael A. Schneider, *Foreign Listings and the Preeminence of U.S. Securities Exchanges: Should the SEC Recognize Foreign Accounting Standards?*, 3 MINN. J. GLOBAL TRADE 301, 301-05 (1994) (describing the difficulties in attracting foreign companies to list on U.S. exchanges while requiring them to use GAAP); see also Eierle, *supra* note 172, at 299-301 (discussing "differential reporting" with different standards within European countries, as well as in New Zealand, Canada, and Hong Kong).

³⁴⁷ Eric M. Sherbet, *Bridging the GAAP: Accounting Standards for Foreign SEC Registrants*, 29 INT'L L. 875, 875-77 (1995) (arguing in favor of requiring foreign firms to comply with U.S. GAAP requirements).

vergence projects).³⁴⁸

At present, the SEC is still considering whether permitting voluntary adoption would complicate the process, or whether it would be a welcome experiment. Judging by SEC Staff Papers and Progress Reports, the Commission is currently focusing on the future of the FASB and on how exactly to adopt IFRS. From a practical point of view, it may be better to resolve these issues first. For instance, if the SEC allowed U.S. companies to voluntarily adopt IFRS but then, when making it mandatory for all U.S. publicly traded companies, decided to move forward with some “carve-outs,”³⁴⁹ this would complicate the process, as the early adaptors would end up having to switch once again, this time to a U.S. version of IFRS. Alternatively, they would be allowed to use IFRS as issued by IASB for the sake of consistency and comparability of their financial statements over the years and forego comparability at the national level. Of course, if the SEC ever decides to adopt IFRS, the ultimate goal should be to adopt them as issued by IASB, without any carve-outs. For the time being, it may make sense to allow voluntary “early” adoption.

4.2. Changing Institutions

4.2.1. The Future of FASB If IFRS Are Adopted in the U.S.

If it is inevitable for the U.S. to fall in line with the rest of the world and adopt IFRS, this raises questions of institutional transition that are to some extent comparable to those encountered in the EU. As was discussed above in section 2, there are some questions concerning how IASB, as a private self-regulatory body on the international level, would be integrated into the U.S. legal system.³⁵⁰ The more practical question is how to transition from the old to the

³⁴⁸ Bertomeu & Cheynel, *supra* note 344, at 808–09 (observing that a possible result of allowing firms to choose their own standard would be “that competing standard-setters would optimally choose to converge and pass the same standard”).

³⁴⁹ See *infra* Section 4.2.1.

³⁵⁰ See *supra* notes 55–60 and accompanying text at Section 2.2.2. (discussing concerns about delegating law making authority to a small, self-appointed, and private body).

new status quo on the factual level. It may be problematic to empower an international organization while undercutting a very powerful national one. The SEC has statutory authority to establish financial reporting standards for publicly held companies.³⁵¹ With the Sarbanes-Oxley Act of 2002, the SEC may recognize “any accounting principles established by a standard setting body” as U.S. GAAP.³⁵² If the SEC decides to adopt IFRS, IASB will in effect take over the current role of FASB as the standard-setting body.³⁵³ Setting aside concerns about delegating power to an international private organization, there has also been some discussion on the future role of FASB.³⁵⁴

The SEC has been mapping out the new roles of FASB depending on various possibilities of IFRS adoption and making it clear – via staff papers and press releases – that there will be a need for FASB even after the adoption of IFRS.³⁵⁵ For instance, in 2011 the then SEC Chair Mary Schapiro expressed her view that FASB

³⁵¹ See, e.g., Securities Exchange Act of 1934, § 13(b)(1), 15 U.S.C. § 78m(b)(1) (1934) (granting the SEC authority to prescribe reporting standards for publicly held companies), available at <http://www.sec.gov/about/laws/sea34.pdf>; see also SEC Study 2003, *supra* note 11 (reaffirming the SEC's role in establishing accounting standards to be used by public companies).

³⁵² 15 U.S.C. § 77s(b)(1) (permitting the SEC to “recognize, as ‘generally accepted’ for purposes of the securities laws, any accounting principles established by a standard setting body” that fulfill certain criteria).

³⁵³ See, e.g., Bratton, *supra* note 63, at 472 (discussing the SEC's Roadmap to achieve mandatory use of IFRS by U.S. domestic issuers); see generally SEC Roadmap, Nov. 14, 2008, *supra* note 4.

³⁵⁴ See, e.g., Bratton, *supra* note 63, at 495–96 (discussing political concerns about mandating IFRS for U.S. companies, arising from the relations between the SEC and IASB); SEC Roadmap, Nov. 14, 2008, *supra* note 4, at 9–10 (outlining the FASB's role in incorporating IFRS into U.S. GAAP); SEC Staff Paper, May 26, 2011, *supra* note 4 at 2–3 (discussing various roles that FASB could serve in implementing a convergence of accounting standards); see also Mary-Jo Kranacher, *FASB Looks to the Future: Standards Setting in the Post-Convergence World*, CPA J., Dec. 2011 (addressing FASB's potential role in a post-convergence world).

³⁵⁵ Until recently, all discussions focused on three main alternatives of allowing IFRS use in the U.S.: adoption, conversion and endorsement. *Adoption* is a switch from U.S. GAAP to IFRS, without converging them first, while *convergence* is a gradual movement from U.S. GAAP to full or near-full IFRS. Finally, *endorsement* is used for the new or amended IFRS before they are formally enacted. See, e.g., *Accounting Standards in the U.S. – Convergence with IFRS*, *supra* note 319 (discussing these four routes to IFRS use in the United States); *USA - IFRS Condone-ment Explained*, IASEMINARS (July 1, 2012), http://www.iaseminars.com/latest/135_usa_-_ifrs_condorsement_explained (outlining the four separate approaches to implementing IFRS in the United States).

would “continue to play a substantive role not only in achieving the promise of high-quality global accounting standards but also – should the Commission decide to move forward with incorporation – in helping to maintain those standards, as well.”³⁵⁶

In light of the plans published by the SEC so far, it seems likely that it will not directly designate IASB as the standard setter. The 2008 Roadmap outlines an “endorsement” mechanism as a possible option that would keep FASB as the “designated standard setter” expected to incorporate all provisions under the IFRS, and all future changes to the IFRS directly into U.S. GAAP.³⁵⁷ For example, Pöschke argues that the most reasonable way of incorporating IFRS could be “by using U.S. GAAP as the mechanism of implementation, i.e. by amending and substantially replacing U.S. GAAP.”³⁵⁸ This way, he claims, the risk of having a dual system of IFRS and U.S. GAAP would be eliminated.³⁵⁹ Most recently, the SEC has been discussing another alternative called “condorsement”³⁶⁰ (a neologism combining “convergence” and “endorsement”), which seems to be similar to EU endorsement process except the fact the endorsed standards will be called U.S. GAAP (or part of U.S. GAAP) rather than IFRS. Arguably, the strongest rea-

³⁵⁶ Mary L. Schapiro, Chairman, SEC, Remarks Before the Financial Accounting Foundation’s 2011 Annual Board of Trustees Dinner (May 24, 2011), available at <http://www.sec.gov/news/speech/2011/spch052411mls.htm>.

³⁵⁷ SEC Roadmap, Nov. 14, 2008, *supra* note 4, at n.31 (describing that “[o]ne of the options would be for the Financial Accounting Standards Board . . . to continue to be the designated standard setter for purposes of establishing the financial reporting standards in issuer filings with the Commission”).

³⁵⁸ Pöschke, *supra* note 28, at 58; *see also* Hail et al., *supra* note 13, at 572-75 (discussing current and proposed implementation and oversight organizations).

³⁵⁹ Pöschke, *supra* note 28, at 58 (describing the “mere formal co-existence of U.S. GAAP and IFRS” while in reality, “U.S. companies would . . . have to apply IFRS rules in all areas”).

³⁶⁰ *See* SEC Staff Paper, May 26, 2011, *supra* note 4 (referencing and explaining condorsement, a possible incorporation approach, which is “in essence an Endorsement Approach that would share characteristics of the incorporation approaches with other jurisdictions that have incorporated or are incorporating IFRS into their financial reporting systems”); *see also* *Accounting Standards in the U.S. – Convergence*, *supra* note 319 (describing “condorsement” as a fourth option first suggested in late 2010 that became favored by the SEC); Paul A. Beswick, Deputy Chief Accountant, SEC, Remarks Before the 2010 AICPA National Conference on Current SEC and PCAOB Developments (Dec. 6, 2010) available at <http://www.sec.gov/news/speech/2010/spch120610pab.htm> (outlining the co-endorsement approach); Wing W. Poon, *Incorporating IFRS into the U.S. Financial Reporting System*, 10 J. BUS. & ECON. RES. 303, 307-08 (2012) (summarizing the SEC’s understanding of the condorsement approach and the subsequent feedback on this approach).

son for advocating a condorsement approach could be that it would maintain the U.S. GAAP system and thus save on administrative costs.³⁶¹ The trouble with this is that altering international standards to suit an individual economy defeats the very purpose of seeking such standards in the first place. Carve-outs would jeopardize precisely the *comparability* of financial statements that was the initial motivation for considering the adoption of a single set of financial reporting standards.³⁶² Moreover, allowing carve-outs would open the door to pressure from politics or local interest groups.³⁶³

Moreover, a special U.S. version of IFRS could be seen as indicating a basic lack of commitment to the idea of an international standard in financial reporting and this, given the clout of U.S. financial markets, could damage the whole international harmonization project worldwide.³⁶⁴ For example, the American Institute of Certified Public Accountants ("AICPA") has warned the SEC about the practical challenges that could limit the effectiveness of the proposed methodology in achieving the SEC's objective.³⁶⁵

No matter how the SEC decides to proceed, it is clear that FASB will have to change and take up a fundamentally different role. With IASB becoming the standard-setting body, FASB will serve as a "facilitator" at best. Most strikingly, the AICPA recommends that FASB's authority should be limited even further. In a comment letter, the AICPA suggests that FASB should focus on public-

³⁶¹ See, e.g., *Accounting Standards in the U.S.—Convergence*, *supra* note 319 (arguing that it "would help companies save on non-value added conversion costs. For instance, they wouldn't have to amend debt covenants to reference IFRS instead of U.S. GAAP.").

³⁶² This problem has emerged in the EU. As an example, IAS 39 (which deals with fair value and hedge accounting) was endorsed with a carve-out. See Colasse, *supra* note 278, at 388 (noting that French banks were responsible for the EU resistance to IAS 32 and 39); *id.* at 390 (discussing the amendment to allow firms to stay within Basel II); Colasse, *supra* note 9, at 33, 40–41 (quoting President Chirac).

³⁶³ See generally Naomi S. Soderstrom & Kevin Jialin Sun, *IFRS Adoption and Accounting Quality: A Review*, 16 EUR. ACCT. REV. 675 (2007) (arguing that institutional settings can drive differences in accounting policy).

³⁶⁴ See *IFRS Perspectives: An Executive Survey*, PRICEWATERHOUSECOOPERS (Dec. 2009), available at <http://www.pwc.com/us/en/issues/ifrs-reporting/publications/index.jhtml> ("A long-term, convergence-only process risks derailing the goal of achieving global standards . . .").

³⁶⁵ See AICPA Recommendations, *supra* note 318 (discussing various practical challenges); see also Goldschmid, *supra* note 31, at 11 (agreeing with the SEC that carve-outs should be used in only very "rare" and "unusual" circumstances).

ly traded companies and the incorporation of IFRS in the United States, while a separate board should be established to develop GAAP for private companies.³⁶⁶ While privately held firms in the United States are not legally required to comply with GAAP, some do so voluntarily in practice to satisfy their creditors and other stakeholders.³⁶⁷ However, applying the complex standards of U.S.

³⁶⁶ The idea of creating a separate body developing U.S. GAAP for private and small businesses has recently gained traction with the possibility of adopting IFRS for U.S. publicly traded companies. A Blue-Ribbon Panel on Private Company reporting was formed to provide recommendations on the future of standard setting for 28 million private companies and small businesses in the U.S. The emphasis of this panel was to address how accounting standards could best meet the needs of the users of private company financial statements. See, e.g., BLUE-RIBBON PANEL ON STANDARD SETTING FOR PRIVATE COMPANIES, REPORT TO THE BOARD OF TRUSTEES OF THE FINANCIAL ACCOUNTING FOUNDATION (Jan. 2011) [hereinafter Blue-Ribbon Panel Report, Jan. 2011], available at http://www.aicpa.org/interestareas/frc/accountingfinancialreporting/pcfr/downloadabledocuments/blue_ribbon_panel_report.pdf (evaluating standard-setting for private companies); Elaine Henry & Oscar J. Holzmann, *Costly Compliance with U.S. GAAP: The Private-Company Dilemma*, J. CORP. ACCT. & FIN. 87, 87 (2012) (detailing the results of the Blue-Ribbon panel and other matters); Barry Melancon, AICPA President and CEO, Private Company Financial Reporting: The Time for Change is Now (May 23, 2011), available at <http://www.aicpa.org/News/AICPATV/Pages/home.aspx?bctid=955338624001&Ca=PCFR&Type=VideoCat> (arguing for differential standards); Floyd Norris, *Proposal Would Create New Accounting Standard-Setter for Private Companies*, N.Y. TIMES, Oct. 4, 2011, at B5 (discussing the Blue-Ribbon panel's proposed modifications).

³⁶⁷ The only state corporate law requiring the use of GAAP is that of California, but even California includes an exemption for firms with fewer than 100 shareholders. CAL. CORP. C. §§ 114, 1501(3) (“[T]he financial statements of any corporation with fewer than 100 holders of record of its shares . . . are not required to be prepared in conformity with generally accepted accounting principles . . .” in particular circumstances); Blue-Ribbon Panel Report, Jan. 2011, *supra* note 367, at 9–10 (discussing the lack of any statutory requirement for private companies to comply with GAAP); Video Webcast: Vincent J. Love & John H. Eickemeyer, *Accountants’ Liability: Litigation and Issues in the Wake of the Financial Crisis – GAAP v. IFRS; Public v. Private Company Accounting; PCAOB AS and GAAS v. ISA* (AM. LAW INST. Sept. 15–16, 2011); Norris, *supra* note 366 (discussing the potential modification of the accounting rules for private companies); see FIN. ACCT. FOUND. BD. TRUSTEES, ESTABLISHMENT OF THE PRIVATE COMPANY COUNCIL, FINAL REPORT (2012) [hereinafter FAF Final Report], available at <http://www.accountingfoundation.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175824045379&blobheader=application%2Fpdf> (suggesting new standards for private companies); CHRISTOPHER NOBES & ROBERT PARKER, *COMPARATIVE INTERNATIONAL ACCOUNTING* 177 (12th ed. 2012) (“[O]nly a small minority of US companies (about 14,000) are SEC-registered and have to obey the SEC’s accounting and auditing rules”); Armour et al., *supra* note 7, at 124–25 (explaining that, although private companies in the U.S. are not required to disclose financial information, many “voluntarily submit detailed financial information to private credit bureaus . . . to gain better access to financing

GAAP created primarily for public companies is often too costly for other private companies, for which these efforts would be futile because the advantages for the ultimate users of their financial statements are minimal.³⁶⁸ Still, a “duality” of FASB and a new board would create a need for yet another mechanism to ensure coordination and cooperation between the two bodies, since having public and private companies reporting under substantially different standards in the same country would not seem to be beneficial. On the other hand, mandating the use of IFRS by *all* companies would place a heavy burden on private and small companies.³⁶⁹ Alternatively, it seems more practical to create a more efficient subcommittee under FASB to work specifically on financial reporting standards for private companies. In the end, the Financial Accounting Foundation (“FAF”) Board of Trustees found this approach more effective and established a new body, the Private Company Council (“PCC”), in May 2012. PCC is intended to improve the process of setting accounting standards for private companies but the proposed changes will be subject to endorsement by the FASB before becoming part of U.S. GAAP.³⁷⁰

in the ordinary course of business.”); Pöschke, *supra* note 28, at 60 (noting that GAAP are “not part of the ‘law’ in a technical sense,” except for certain SEC regulations, and that their authority is based only on recognition by the SEC); *see also* GARY JOHN PREVITS & BARBARA DUBIS MERINO, A HISTORY OF ACCOUNTANCY IN THE UNITED STATES: THE CULTURAL SIGNIFICANCE OF ACCOUNTING 69–73, 365–67, 376–78 (1998) (explaining that the maintenance of rigid accounting standards is consistent with business success). *See generally* Robert Tie, *The Case for Private Company GAAP*, 199 J. ACCT. 27 (2005) (demonstrating that many stakeholders value GAAP because they allow stakeholders to compare company performance over time).

³⁶⁸ FAF FINAL REPORT, *supra* note 368, at 35 (discussing industry participants’ views on the FAF proposal); Stuart Moss & Timothy Kolber, *Private Matters: Proposed Council to Improve Standard Setting for Private Companies*, 18 DELOITTE: HEADS UP 1, 2 (2011), available at http://www.deloitte.com/assets/Dcom-United-States/Local%20Assets/Documents/AERS/ASC/us_aers_headsup_101011.pdf (discussing how a “one size fits all” standard may strain the resources of smaller, private companies).

³⁶⁹ For example, both IASB and FASB have been shifting toward a fair-value-based accounting approach. Thus, compliance with these financial reporting standards requires companies to report assets and liabilities at fair value rather than historical cost. The fair value standard increases the cost of compliance because it demands periodic valuations of many financial statement items. While having the information according to fair value is important for public company investors, private companies seem to see it as a costly burden without much benefit because creditors and other users of private company financial statements are interested in cash flow and a company’s ability to pay its debts.

³⁷⁰ *See* FAF FINAL REPORT, *supra* note 368, at 10 (“If the FASB makes a final

Finally, a transnational harmonization of accounting standards may have benefits on the level of private firms, which is why the IFRS Foundation has already created a subcommittee to prepare a version of IFRS for SMEs.³⁷¹

4.2.2. Funding the IFRS Foundation from United States Sources

The funding of the IFRS Foundation, an international private non-governmental organization, has so far been a big impediment for the adoption of IFRS in the United States. The reason is twofold. First, the SEC is already funding a standard setting body, FASB, and has not yet decided about the future of the FASB. If IFRS are adopted, the SEC will have to decide which institution will receive the funds. Second, it is not clear whether the SEC has the power to directly transfer funds to IASB, even if IFRS are adopted for U.S. issuers.³⁷²

Currently, the SEC funds FASB through an annual levy of accounting support fees from issuers of U.S. securities; however, it is not clear whether these funds could be transferred to an interna-

decision to endorse, the exceptions or modifications will be incorporated into U.S. GAAP.").

³⁷¹ See, e.g., GRANT THORNTON, WHO SHOULD SET FINANCIAL REPORTING STANDARDS FOR PRIVATE COMPANIES? 1-3 (2011), available at http://www.gt.com/staticfiles/GTCom/Audit/Assurancepublications/PSG_Standards-For-Private-Companies-WP_FINAL.pdf (noting the heated debate about private company financial reporting, and that 73 countries were then considering the adoption of IFRS for SMEs); Glenn Alan Cheney, *Private Company Accounting Standards – New Road or Same Old Path?*, FIN. EXECUTIVES INT'L (Mar. 2012), available at http://www.financialexecutives.org/KenticoCMS/Financial-Executive-Magazine/2012_03/Private-Company-Accounting-Standards--New-Road-or-.aspx (summarizing various views on special standards for private companies); Andy Thrower, *Should It Be a 'Big GAAP' or 'Little GAAP' for Private Companies?*, FIN. EXECUTIVES INT'L (Mar. 2010) (arguing that the GAAP framework should apply to all U.S. companies, large and small, with additional disclosure requirements for large companies); Bruce Pounder, *The Big Risks of Little GAAP*, CFO.COM (Dec. 2010), <http://ww2.cfo.com/accounting-tax/2010/12/the-big-risks-of-little-gaap> ("Introducing an additional set of standards without attaining pervasive acceptance and successful implementation would increase the diversity of standards used by private U.S. companies. In turn, this would further reduce comparability across reporting entities while increasing the complexity and cost of financial-statement preparation, auditing, and analysis.").

³⁷² SEC Final Staff Paper, July 13, 2012, *supra* note 4, at 56 ("[T]he Commission may be limited from directly funding the IFRS Foundation without an appropriation request of Congress.").

tional body such as IASB.³⁷³ The Sarbanes-Oxley Act of 2002 requires the SEC “to pay for the budget and provide for the expenses of [the] standard setting body, and to provide for an independent, stable source of funding for such body.”³⁷⁴ The annual funding of the FASB is provided only after the SEC annual review of additional sources of revenue and the budgets of the FAF³⁷⁵ and the FASB as well as the annual review of the FASB’s proposed accounting support fee.³⁷⁶

Not accepting contributions from the accounting industry is essential in this “review and fund transfer” process of the SEC because independent source of funding is believed to ensure the independence of a standard setting body.³⁷⁷ Up until Sarbanes-Oxley, FASB and its predecessors heavily relied on contributions from the large accounting firms, which affected at least the outside perception of independence.³⁷⁸ IASB faces the same issue because the IFRS Foundation relies heavily on contributions from the large accounting firms, which contributed approximately twenty-five percent of its 2012 revenue.³⁷⁹ Needless to say, the SEC is concerned that the adoption of IFRS might take capital markets back to

³⁷³ *Id.* at 52–58 (outlining various approaches and issues relating to funding), at 56 (citing 31 U.S.C. § 1341(a)(1)(B) (Antideficiency Act): “An officer or employee of the United States Government or of the District of Columbia government may not . . . involve either government in a contract or obligation for the payment of money before an appropriation is made unless authorized by law”); *see also* Oct. 2012 IFRS Foundation Report, *supra* note 4.

³⁷⁴ 15 U.S.C. § 7219 (prescribing the funding of the SEC).

³⁷⁵ *See supra* note 64 (discussing the FAF and the FASB).

³⁷⁶ SEC Final Staff Paper, July 13, 2012, *supra* note 4, at 55 (noting that, after reviewing the budgets of FAS and FASB, “the Commission determines whether the proposed annual accounting support fee is consistent with Section 109 of the Sarbanes-Oxley Act”).

³⁷⁷ *Id.* at 55, 57–58 (“The Commission reviews any additional sources of revenue, and the FAF represents that neither the FAF nor the FASB accept contributions from the accounting industry.”).

³⁷⁸ Bratton, *supra* note 63 at 477 (“[IASB] made ends meet for 2009 only as a result of a £5.5 million commitment by the Big Four Accounting Firms. Red flags unfurl accordingly: accounting standards bear critically on the audit process, and hence, audit firm earnings.”) (footnote omitted); Anne B. Fosbre, Ellen M. Kraft & Paul B. Fosbre, *The Globalization of Accounting Standards: IFRS Versus US GAAP*, 3 GLOBAL J. OF BUS. RES. 1, 63–64 (2009) (noting that the Accounting Principles Board was responsible for standard setting from 1959–1973, and that the Board “was criticized by industry and government for their lack of independence.”).

³⁷⁹ SEC Final Staff Paper, July 13, 2012, *supra* note 4, at 58 n.279 (noting that international accounting firms contributed twenty-six percent of the 2011 budget of the IFRS Foundation).

pre-Sarbanes Oxley days in terms of the standard-setter's financial dependence.³⁸⁰

Dependence on large accounting firms looks like a hurdle that could be easily overcome if the United States funds the IFRS Foundation's budget in proportion to the size of its economy.³⁸¹ According to the IFRS Foundation Report, the present U.S. contribution corresponds to less than one third of what it would pay if the amount were proportionately based on GDP.³⁸² Considering the fact that around 25% of the total seats in the Foundation's governing bodies are held by U.S. individuals (while U.S. contribution accounts only for 8% of national government contributions), this criticism is understandable. The EU currently provides core funding to the Foundation.³⁸³ Given the questionable authority of the SEC to fund an international body,³⁸⁴ the strong American representation at IASB and the IFRS Foundation may be in jeopardy.³⁸⁵ The SEC, seeing what is at stake, recently made a \$3 million special contribution to support the completion of the convergence project.³⁸⁶ While this is a clear sign of continued commitment by the SEC,³⁸⁷ its current strategic plan for the next four years sends

³⁸⁰ *Id.* at 54–55 & n.263; see Cox, *supra* note 18, at 950; Walter Mattli & Tim Büthe, *Global Private Governance: Lessons from a National Model of Setting Standards in Accounting*, 68 L. & CONTEMP. PROBS. 225, 254–55 (2005).

³⁸¹ Oct. 2012 IFRS Foundation Report, *supra* note 4, at 8, 24–25.

³⁸² *Id.* (noting that GDP is the primary indicator used by the IFRS Foundation to assess the funding expectations of a country).

³⁸³ See Guersent, *supra* note 37, at 2 (noting that the European Commission “decided to enhance EFRAG's resources by co-financing it from 2010.”).

³⁸⁴ See *supra* note 373 and accompanying text (outlining issues to do with the SEC funding an organization like IFRS).

³⁸⁵ See, e.g., Guersent, *supra* note 37, at 4–5 (describing the growing frustration by the EU given continued hesitance in the U.S. and noting the belief that “the monitoring board should first be composed exclusively of countries using IFRS on their domestic market and second be expanded to major emerging economies applying IFRS”); see also *Parliament to Challenge International Accounting Standards*, EURACTIV.COM (May 8, 2013, 8:53 AM), <http://www.euractiv.com/euro-finance/parliament-challenge-international-news-519598> (“Lawmakers are also annoyed that the United States, which retains a strong influence on the IASB, has not itself adopted the IFRS.”).

³⁸⁶ News Release, Fin. Acct. Found., Financial Accounting Foundation to Provide Up to \$3 Million to IFRS Foundation to Aid Completion of Joint IASB Projects (Jan. 28, 2014), *available at* http://www.accountingfoundation.org/cs/ContentServer?pagename=Foundation%2FFAFContent_C%2FFAFNewsPage&c=FAFContent_C&cid=1176163774653 (confirming the financial support of the FAF following consultation with the SEC).

³⁸⁷ Hoogervorst, *supra* note 22, at 3 (“[T]he US Financial Accounting Founda-

mixed signals.³⁸⁸ The draft plan does not mention IFRS, but cryptically says that the SEC will “consider . . . whether a single set of high-quality global accounting standards is achievable.”³⁸⁹

5. CONCLUSION

In this article, we have surveyed the debate about the introduction of IFRS in the United States and compared it to the one in Europe. Contrary to what a casual outside observer might believe, IFRS have not completely taken over European accounting, even though this set of standards has considerably pushed back traditional national accounting systems during the past decade. Nevertheless, national accounting traditions largely persist in parallel, in part because they are very different from IFRS in content and purpose. The debates about IFRS, which were hotly waged in the years leading up to their mandatory introduction for the consoli-

tion gave a clear sign of continued commitment to the joint work of the IASB and the FASB in finalising the remaining convergence projects by making a \$3 Million dollar financial contribution to our work.”); *Is SEC on the (IFRS) Road(map) Again? FAF Contributes \$3 Million to IFRS Foundation – Update 2*, FIN. EXECUTIVES INT’L (Jan. 29, 2014, 1:07 PM), http://www.financialexecutives.org/KenticoCMS/FEI_Blogs/Financial-Reporting-Blog/January-2014/Is-SEC-on-the-IFRS-Roadmap-Again-FAF-Contributes-3.aspx (discussing what can be inferred about the SEC’s IFRS plans, given the FAF funding decision, made in consultation with the SEC); *but see* Email from Carlos Johnson, NASBA Chair & Ken Bishop, NASBA President and CEO, to Jeffrey J. Diermeir, FAF Chairman & Teresa S. Polley, FAF President and CEO (Feb. 14, 2014), *available at* http://www.accountingfoundation.org/cs/ContentServer?c=Document_C&page name=Foundation%2FDocument_C%2FFAFDocumentPage&cid=1176163831522 (criticizing and questioning the FAF contribution to the IFRS foundation).

³⁸⁸ SEC, Strategic Plan: Fiscal Years 2014–2018, Draft for Comment (2014), *available at* <http://www.sec.gov/about/sec-strategic-plan-2014-2018-draft.pdf> (detailing the proposed direction of SEC from 2014–2018).

³⁸⁹ *Id.* at 8 (linking this to “the increasingly global nature of capital markets”); *see also* Ken Tysiac, *SEC Plans to Consider Whether Global Standards Are Achievable*, J. ACCT. (Feb. 3, 2014), *available at* <http://www.journalofaccountancy.com/News/20149536> (commenting on the Draft SEC Strategic Plan, with particular focus on the SEC’s plan that “a single set of high-quality global accounting standards is achievable”); Emily Chasan, *SEC’s New Strategic Plan Backs Away from IFRS*, WALL ST. J. (Feb. 4, 2014), <http://blogs.wsj.com/cfo/2014/02/04/secs-new-strategic-plan-backs-away-from-ifrs> (commenting that the “tone” of the Draft SEC Strategic Plan “appeared to back away from the possibility that U.S. companies would one day file financial reports under International Financial Reporting Standards”).

dated accounts in publicly traded firms, have not ceased and even surged to some extent after the financial crisis. In the United States, whose GAAP are firmly within the capital-market-oriented Anglo-Saxon tradition, differences to their younger sibling IFRS are much smaller, which is why hurdles to introduction should be so as well. Nevertheless, the United States, which originally pushed IFRS internationally, is still hesitating. While the SEC sidelined the issue, we have suggested that introducing IFRS, even on the mandatory level, should not pose insurmountable.