Chapter 16
Commentary. Current State and Future Challenges of the IFRS: Some Thoughts

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16.1 Introduction

My first words are to congratulate and thank Roberto, Stuart, and Joshua for bringing this most interesting and timely book on Accounting Regulation into the public domain. Indeed accounting regulation is a major issue, not only for us, the accountants, but also for society as a whole. Despite this, I often have the impression that there is a real lack of understanding about its implications and links with other institutions that shape the real economy. Moreover, the present economic crisis has highlighted the varied opinions on the role accounting standards and financial accounting in the economy. Should they be oriented to the financial market? Or should they act as another instrument to ensure economic and financial stability?

I also very much appreciate the chance I have been given to write a short piece for the forum. Of course, this should be related to the general topic of the book, an area I enjoy immensely as, after all, it makes the core of my own research and teaching activities. Therefore, I intend to share some of these more personal thoughts on the current state of affairs as well as the future challenges facing accounting regulation, and in particular the International Financial Reporting Standards (IFRS).

The main objective of the IFRS Foundation as stated in its constitution is to provide high quality standards, which help to prepare information that meets the user's needs (IFRSF 2010); it focuses on the needs of a particular group of users, investors, and mainly on capital providers. However, it would seem that this is frequently ignored or at least forgotten in the discussions about the role and success of the IFRS. With this idea in mind, principle-based standards are developed, and some jurisdictions have adopted the standards voluntarily. As frequently mentioned principle-based standards are a double-edged sword. While

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some discretion is given to managers which allows them to convey private information, other incentives may also come into play.

Bearing this in mind, next I wish to explore both sides of the previous statements: the development of standards and the decision to adopt them. After that I will insist on two-related aspects that drive the final success of the aforementioned objective: implementation and enforcement. I will conclude with some final remarks.

16.2 The Development of the IFRS

The production of the standards lies with the International Accounting Standards Board (IASB) itself, as this is its main task. To achieve this, the Board is composed by a team of excellent independent experts, selected by the Trustees of the IFRS Foundation. This team is publicly accountable to a monitoring board of capital market authorities and other regulators; a strong due process has been established to guarantee the standard-setting procedure, and make it transparent for both the standard-setter and the participants who provide both input and feedback. Although preparers have traditionally been very active in the standard-due process due to their incentives to lobby, other stakeholders have been less interested (Dechow et al. 1996; Ang et al. 2000; Hill et al. 2002; Jorissen et al. 2012; Giner and Arce 2012).

In particular I want to highlight the scarce participation of academics, though this is not altogether surprising, as tends to happen with other standard-setters. In this case incentives fail to encourage academics to participate, on the contrary we are more often than not most concerned with getting published in highly ranked journals, and so spending time on other activities is frequently perceived as mere time wasting … Despite this, or more probably because of this, the Trustees of the IFRS Foundation in its Strategic Review have recommended establishing or facilitating the establishment of a research capacity that could be based on a combination of internal and external intellectual resources, including a more active engagement of the academic community. This will allow the IASB to rely on evidence to support its decisions and to persuade those who use IFRS that the IASB has made the right choices between competing solutions when developing standards.

Indeed given that academics are the main experts in research activity, it would only seem quite natural to rely on us to perform this task. Larson et al. (2011) provide details about the role of academic research in the development of standards and encourage us to participate in the development of IFRS. Although it is up to individuals to react and participate in the standard-setting process, either by responding to the call for responses to discussion papers and exposure drafts, or by showing an interest in the calls of the IFRS Foundation to occupy a temporary position (such as academic or research fellow), there is also the possibility to act in a more organized way, and this is what the European Accounting Association

Financial Reporting Standards Committee (EAA FRSC) is doing. This committee has been providing input to IASB, as well as European Financial Reporting Advisory Group (EFRAG), in the form of comment letters, but has also liaised with IASB and EFRAG, and now includes two liaison members who help us remain in permanent contact with them.

Another interested group that deserves special attention is the standard-setters' group; in Chap. 13 we pay attention to their role (Giner and Arce 2013), but here I want to highlight some aspects of the new group just promoted by the IASB, namely the Accounting Standard Advisory Forum (ASAF). ASAF mainly aims to provide support to the IASB on technical issues. Indeed national standard-setters and regional bodies are experts on accounting issues, but in my view there is another important aspect that could leverage their input in the process. Based on their good knowledge of the institutional arrangements in their own jurisdictions and on how the proposed standards could affect them, they are in a unique position to evaluate the impact of the changes, So, sharing this information could only help the IASB to make better-informed decisions.

Despite the previous comments, it is important to keep in mind that the IASB is the standard-setter and the purpose of the IFRS is to have good information for the capital markets, so that the unintended consequences of the standards should not drive the discussions, leaving aside the actual decisions. As I see the role of the Forum, it could make local bodies engage more easily with their own stakeholders in order to accept and use the IFRS following the IASB's objectives. In this way I believe it could give them a real sense of ownership of the standards, To the extent those bodies have endorsement powers; ASAF could also be useful to facilitate the adoption of IFRS without any carve out or delay, I will insist later on these problems.

16.3 The Decision to Use the IFRS

The decision to adopt IFRS is made at the national or jurisdiction-level as the IASB has neither the power to impose its standards nor to enforce its proper application. As some authors have pointed it is a "leap of faith" that the adoption of IFRS will bring the desired output of improved decision-making, and indeed this was the case when the first followers, the EU, Australia, and New Zealand, made that decision. More importantly, and with reference to the EU, Pope and McLeay (2011, p. 211) posit "the Commission has placed considerable trust in the ability of the primary system of devolved enforcement to deliver uniformly consistent high quality financial reporting." This brings me to the role of enforcement and each country's institutions in shaping the final content of financial information. However, before that I would like to make a brief comment on the politics of the accounting standard-setter process.

As Bushman and Landsman (2010) argue, the economic recession has brought into sharp focus the reality that the regulation of corporate reporting is just one piece of a larger regulatory configuration. The pressure of prudential regulators, financial institutions, and some national standard-setters, who put the emphasis on the unintended consequences of the standards, might endanger the ability of the IASB to maintain its role as producer of standards that promote corporate transparency to support market discipline and capital allocation. Indeed there is strong pressure on the IASB to accommodate the requirements of the prudential regulators, but this strategy contradicts its own constitution. Moreover, this discussion questions the extent to which those authorities who adopted IFRS were aware of the real impact of their decision. As mentioned in the introduction, this suggests there is a real lack of understanding about the implications and links of accounting regulation with other institutions that shape the real economy; and it is not clear whether both objectives, capital market transparency and prudence, cannot be achieved simultaneously.

16.4 The Implementation and Enforcement of IFRS

Implementation and enforcement are the key aspects to the achievement of high quality global accounting information as Leuz (2010) and Brown (2011), among others, sustain. It can be argued that to some extent the main difficulty nowadays is not to produce highly technical accounting standards but to guarantee they are used and enforced properly. Although none of these aspects are under the control of the IASB, in a way they are key to judging the success of the IASB. Having said that, it would not be acceptable to discard the idea that in order to achieve high quality information, one must first start with high quality standards.

Nowadays IFRS are used in many jurisdictions. Philip Danjou (2013), a current Board member, has recently confirmed that more than 100 jurisdictions require or permit the application of IFRS for financial reporting, and two thirds of G20 countries have adopted IFRS. However, the approaches followed to adopt them substantially vary from one country to another. In some countries the standards are directly applied, such in as South Africa, while in others there is an endorsement process, as in the European Union. This allows some not to accept a given standard or even some paragraphs of the standards (as the *carve out* made in IAS 39), as well as delay in the endorsement decision (as happened with IFRS 9), or even the delay in the application of a standard (such as with IFRS 10, 11, and 12, as well IAS 27 and 28). In some countries IFRS have been imposed for certain types of companies and accounts, consolidated accounts of listed companies in the EU, while in others, such as Australia individual accounts, as well as nonlisted companies are also affected. In addition there are some countries that allow IFRS for foreign companies, such as in Japan and the US. Finally other countries have convergence programs, but they are far from real adopters as what they finally decide could be rather different to the full IFRS package. I am not implying that these programs are useless, as according to the constitution, the convergence of national accounting standards and IFRS is a strategy to promote and facilitate adoption of IFRS, which is another objective of the IFRS Foundation. This scenario introduces serious doubts about the use of full IFRSs in the world. Indeed that IFRS have been accepted so widely is an impressive achievement of the IASB, and its predecessor the IASC, but it is necessary to keep the mind clear and think about the real use of IFRS.

Although there is an array of studies that confirm the advantages of using IFRS in terms of improved efficiency of capital market operations and promotion of cross-border investment, there is the perception that the IFRS benefits go together with a framework that encompasses legal protections, competent professionals, and adequate monitoring and enforcement (see Tarca 2012 for a good summary of recent research). Thus, there is a growing stream of literature that questions the possibility of obtaining the desired achievements unless there are further changes in the institutions (Hail et al. 2010; Leuz 2010; Walker 2010; Isidro and Raonic 2012). In their view, due to the role of the country's institutional infrastructure, unilateral changes in accounting standards (such as IFRS adoption) may not yield the desired outcomes. In fact Landsman et al. (2012) found that IFRS firms' accounting amounts have greater comparability with those of US firms when IFRS firms apply IFRS than when they apply non-US domestic standards. However, comparability is generally greater for firms that adopt IFRS mandatorily, common law firms, and firms in countries with high enforcement. Even within the most harmonized context, the European Union, Pope and McLeay (2011) confirm that although some of the benefits from increased transparency appear to have been realized, the results are far from uniform due to heterogeneous preparer incentives and differing enforcement mechanisms in member states.

Following this line of argument Wysocki (2011) states that the advantages of IFRS compared with local standards are not evident in countries that have evolved different institutions and thus lack the necessary infrastructures to support the effective application and enforcement of the uniform global standards. Moreover, Ball (2006) argues that as long the incentives of preparers and enforcers remain primarily local, there are fundamental reasons for being skeptical about uniformity of implementation of the standards. Having said that, it is important to keep in mind that this is a real challenge for the IASB as the constitution also includes the following objective: "to promote the use and rigorous application of those standards." The challenge is how to achieve it given the lack of enforcement power in the different jurisdictions. Perhaps as previously mentioned, the strategy to launch the new ASAF could help to advance this objective.

16.5 Final Remarks

To conclude I want to insist on a couple of ideas mentioned above. First of all IFRS are developed to improve the transparency of financial information in order to help investors, so other alternative objectives, as well as the unintended consequences of the information should be left aside in the discussions. Second the IFRS's adoption will not bring the desired impact if there are no further changes in other institutions, and thinking of the EU, the obvious one must be enforcement. At times one has the impression that too much time and effort is being wasted unless a more unified enforcement takes place within the EU.

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