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Gregory Heem

► **To cite this version:**

Gregory Heem. International accounting standardization: the institutional legitimacy of a private standards setters. 2007, 14 p. halshs-00856207

HAL Id: halshs-00856207

<https://shs.hal.science/halshs-00856207>

Submitted on 30 Aug 2013

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International accounting standardization : the institutional legitimacy of a private standards setters

Grégory HEEM
Maître de conférences en Sciences de Gestion
University Paris XIII

ABSTRACT : The objective of this paper is to analyse the sources of legitimacy of the producing organizations of accounting standards. Firstly, we examine the need for harmonisation of accounting standards in particular to maintain the confidence of investors and savers in the financial and economic system. Secondly, the paper presents the internal and external sources of legitimacy and analyses the legitimacy of the International Standard Accounting Board (IASB).

KEY WORDS : International Financial Reporting Standards, IFRS, IASB, Legitimacy, Standardization, International accounting.

Cahier de recherche du CREGEM, n°02/2007, Université Paris 13.

1. Introduction

Recent scandals have brought the issue of banking and financial sector regulation to the forefront. In France and in the US, legislators have reacted by introducing new legal measures (French law on the financial security, Sarbanes Oxley Act).

However, accounting standards have a major impact on the information published by companies distributing securities to the public and thus contribute to the efficient operation of the sector. Consequently, the public authorities cannot afford to overlook developments in applicable standards.

Before going any further, it would be appropriate to explain the meaning of some of the concepts or expressions used in this article. The word “norm” or “standard” comes from the Latin “norma” which means measure or rule. However, this does not explain how standards acquire legal status and thus raises questions as to the foundation for their legitimacy. Kelsen (1934) considers that the legal bearing of a standard resides in the fact that a sanction is applied in the event of a violation.

Indeed, this criterion is traditionally used as the basis for the legality of a standard, which is in turn defined as the possibility of recourse to a judge or arbitrator to impose its application. Note that in accounting, professionals frequently distinguish between general accounting principles and accounting standards. The latter “are based on general accounting principles and are the means by which these principles are applied”. We will therefore use the expression accounting rules to designate the set of principles and standards which apply to accounting. These accounting rules also meet the criteria for legal standards described above.

Yet the likelihood of a law being respected is increased if it has been agreed on the basis of general consensus. This is the key issue of accounting standardisation¹, the need to establish a common ground between professionals and legislators that will serve the interests of the majority. The purpose of this paper is to analyse the legitimacy of the IASB to produce accounting standards. The paper starts with a discussion about the need for harmonisation of accounting standards. Then we analyse the conditions of international legitimacy for the production of standards, at last we apply these conditions to the IASB in order to appreciate his legitimacy.

2. The need for harmonisation of accounting standards

Accounting standards play an important role in the supervision of companies. They allow third parties to assess the financial health of a company and provide investors with useful criteria on which to base their investment decisions. Accounting is designed to keep a trace of the company’s activities and provide a representation of its wealth and assets. Consequently, the contents of accounting standards can both weaken and reinforce the control exercised over a company by modifying the reporting obligations which it must observe. Harmonisation is indeed vital to ensure the effective operation of the market and the interests of the majority are compromised by the increasing emergence of diverse standards and the obvious risk of contradictions.

Given the importance of the issues at stake of the accounting standards, the State justifiably has a major role to play. With the disappearance of international boundaries, national rules alone cannot ensure that the interests of the majority are respected. Harmonisation can satisfy individual interests by ensuring the market functions smoothly, but can also help to respect

¹ Standardisation can be defined as the unification or homogenisation of the applicable rules.

the interests of the majority. In this context, accounting standards set techniques for company valuations which enable external observers to monitor their activities. Accounting standards are thus essential tools in corporate supervision, designed to meet the objectives imposed by the interests of the majority.

Although the interests of the member States may vary, they do share a number of common objectives : protection of investors, stability and security of the banking and financial system and the fight against organised crime and the financing of terrorism. These aims cannot be achieved at national level alone, and at the very least imply the application of a standard body of rules at international level.

While it is justifiable in the interests of the majority for corporate activities be subject to certain obligations, in practice this requires techniques and tools to collect information on corporate operations and verify that the companies in question are actually meeting their established obligations. In this respect, accounting documents provide information which can be used to assess the management of a company and thus guide investors and partners in their decisions, and to detect any breaches in the law. Consequently, accounting standards ensure external parties have access to information on the management of a company.

As indicated by Jean-Louis Fort², the main problem in the banking sector is not how to assess the intrinsic value of an establishment for an unsolicited takeover, but how to guarantee that the establishment continues to operate and respect its commitments. Therefore, IASB standards, and in particular those relating to fair value, appear to place the interests of the shareholder before those of the other stakeholders such as the employees or clients, in as much as the main aim of shareholders is to be able to compare the performance of their investment in any given sector. The European Commission has supported IASC and IOSCO efforts to create a common set of standards for financial reporting, applicable internationally for stock market listing. This harmonisation of accounting standards creates better conditions for achieving the objectives of the Community authorities. The European directive on market abuses confirms that legislation concerning insider trading and market manipulation has the same objective: to ensure the integrity of financial markets within the Community and reinforce investor confidence (Colasse and Standish, 2004). It also highlights the fact that current Community legislation has several loopholes which could leave scope for illicit behaviour that would affect public confidence and the functioning of the markets³. One of the conditions for achieving this objective is a tighter control of companies which have access to the financial markets. And accounting standards are a means of improving this control, by strengthening obligations for financial reporting to third parties.

This initiative can be explained by the debates which have arisen between regulatory authorities and accounting professionals over the application of certain international standards. A good case in point is standard IAS 39 which stipulates the valuation of financial

² Interview with Jean-Louis Fort, secretary general of the French banking commission, in n°440 of the *Revue Française de Comptabilité*, January 2002, pp. 40-47.

³ The directive stipulates that the States must organise a professional hearing on the modification of national legislation, but it reassures the public authorities by stating that the States must entrust the application of the provisions adopted under this directive to a single administrative authority. The directive stipulates that the States must organise a professional hearing on the modification of national legislation, but it reassures the public authorities by stating that the States must entrust the application of the provisions adopted under this directive to a single administrative authority.

instruments at fair value⁴. Admittedly, IAS 39 does pose a number of problems, notably for banks, which, as we have already mentioned, are currently subject to international standards.

The banking and financial sector offers a particularly apt insight into the issues at stake in accounting standardisation. Indeed, the provision of comprehensive and reliable information to investors is a vital condition for companies wishing to access financial markets. In an initial public offering, savers and investors need reliable and objective information on the activities and financial health of the company on which to base their investment decision, while the company in question must offer minimum financial guarantees. In addition, the regulatory authorities must have access to all the information they need to assess the activities of the company if they are to exercise their powers effectively. In this context, accounting documents have a vital role to play as they provide the vast majority of this information.

The change in accounting practices as a result of the switch to IAS/ IFRS standards will have a major impact on European companies. In fact, this development, implies changes at various levels. Firstly, in the philosophy of standards: international standards place substance over form, which implies not so much following the standards to the letter, as respecting the spirit in which they were written. It is interesting to note that this philosophy is not found in US national accounting standards (US GAAP standards) which tend to list an infinite number of options. Secondly, the balance sheet approach will take priority over the income statement, even though, under IAS standard 1, financial reports will still include an income statement. Furthermore, there is a risk that company accounts will become more volatile (financial instruments are booked at fair value (IAS 39), stock options are booked as expenses and the amortisation of goodwill is replaced with an impairment test). The concerns of the banks and insurance companies were that the proposals would create unnecessary volatility in reported profits and discourage sound risk management practices (De Lange and Howieson, 2005). Supporters of these standards, however, stress that accounts will no longer reflect the past, but provide a better vision of the present and a sound indication of the future.

However, the issues at stake in accounting standards go beyond the interests of individual companies. Indeed, this information is not only vital for shareholders and savers but also, more generally, for all ends of the economic spectrum (Pesqueux, 2003). The economic health of a company concerns its shareholders, employees and partners equally. Changing the scale used to assess financial information for all companies has much wider implications due to the role companies play in economic development. In order to maintain the financial and economic stability of the State, it is vital that investors have confidence in the financial information they receive, hence the need for reliable and objective tools with which to assess the value of a company. In this respect, the internationalisation of accounting standards concerns the State not just as a public authority intervening to regulate economic sectors, but also as a shareholder in public companies.

The harmonisation of accounting standards is vital in order to compare companies within a single market where capital can circulate freely. On the one hand, the investment of savings in companies is an essential factor in ensuring a country's economic development. However, in order for investors to decide whether to allocate their funds, they need reliable information on the company in question. Accounting standards are a guarantee that they have access to the

⁴ The idea here is that the concept of historical cost is no longer appropriate for the current economic context. "Fair value: the amount for which an asset can be exchanged or a liability settled, between two willing and informed parties as part of a transaction carried out under normal conditions of competition."

details they require. Indeed, the contents of these standards will affect the image an investor has of a company's financial health, and determine whether the financial information disclosed by a company can be deemed reliable, and thus plays an important role in safeguarding the interests of the investor or saver.

Standards help to maintain the confidence of investors and savers in the financial and economic system. Consequently, given the importance of accounting standards for economic stability and the operation of financial markets, the intervention of the public authorities is a necessary condition. The State must impose legal constraints which guarantee the credibility, accuracy and reliability of the financial information disclosed by companies. It is therefore understandable that the French public authorities have taken an active interest in the auditing profession which supervises accounting practices and their compliance with the applicable regulations.

At the publication of a series of reports in October 2002, the President of the OICV technical committee declared that "investor confidence is a basic condition for the correct operation of international financial markets. This confidence is based on their ability to access reliable and credible information when deciding how to allocate their capital." The OICV stresses that the affirmation of these principles at an international level will provide a specific response to the difficulties underscored by the regulators and brought to light by the bankruptcies of a number of major groups⁵.

After regarding the outstanding importance of harmonization of the international accounting standards, we'll now study the legitimacy that could have private organization to produce such standards.

3. The Legitimacy of the IASB

At international level, the legal framework may be set jointly by a number of different organisations, but the main role in the creation of standards falls to the IASB. However, as the standards it implements have an impact on the functioning of the financial markets, the IASB⁶ works in conjunction with the IOSCO⁷. With the rapid rise in financial markets, IOSCO provides regulators with a vital forum for information exchange and for the study of developments which may be required in their activities or function. It endeavours to define standards which improve financial transparency for investors and the quality of information on company solvency submitted to the regulatory authorities.

The IASC (International Accounting Standards Committee) was created in 1973 by representatives of professional accounting associations from various countries. The purpose of the IFRS is to provide information useful for investment decisions of capital suppliers (IASB Framework).

⁵ Financial reporting must be continuous. It must respect the rules stipulated in accounting standards, the standards established by the regulators, market listing rules, and corporate reporting obligations under the principles of accurate and faithful information. The Technical Committee has developed a number of principles for financial transparency which complement the Standards relating to reporting in a public offering, published by IOSCO in September 1998. It is vital that auditors be independent and the conditions under which they exercise their activity effectively supervised to ensure the faithfulness and integrity of the accounting information provided.

⁶ In April 2001, the IASC became the IASB (IAS Board) and new IAS standards were renamed IFRS (International Financial Reporting Standards).

⁷ International Organisation of Securities Commissions.

The IASC has a series of structures which ensure it maintains a degree of autonomy from the bodies which govern the profession and from the financial market regulators, and also guarantee a rigorous procedure for the drafting, interpretation and revision of standards.

On May 24, 2000, it underwent substantial reform with the adoption of new statutes⁸. Its technical role was separated from its organisational and promotional activities, and the Committee itself was converted into a foundation administrated by some “Trustees”. The purpose of this IASC Foundation (IASCF) is to develop a single body of high quality, comprehensible and practically applicable standards in the interests of the general public, to oblige companies to submit good quality, transparent and comparable information in their financial statements in order to assist participants on global capital markets in their economic decisions. The IASC Foundation also promotes the widespread use of these standards and helps to integrate existing national and international standards into high quality solutions.

The IASB (International Accounting Standards Board) works under the aegis of the IASC Foundation and is responsible for preparing, adopting and modifying international accounting standards. It also develops⁹ a set of accounting rules designed to provide comparability of company accounts, and thereby increase their transparency.

The IFAC (International Federation of Accountants) also plays a role as it aims to develop and promote a unified global accounting profession, governed by a harmonised body of standards¹⁰. Its full members are professional accounting associations recognised by law. However, both the IASB and IFAC are private bodies, which raises questions as to the basis on which private individuals can justifiably create legal standards.

At their meeting in Paris on 21 June 2005 the Trustees of the IASC Foundation approved amendments to the organisation’s constitution which governs the IASC Foundation’s operational arrangements. These changes are important to reinforce the IASCF/IASB legitimacy.

The trustees have made several changes in the constitution to enhance the organisation’s accountability

⁸ It originally had a Board comprising two representatives of thirteen countries, selected by the IFAC, and the representatives of four organisations with an interest in financial reports. The Board decided on the subject of the standards and voted on their approval. Aside from these members, the Board also included observers from the European Commission, the FASB and IOSCO. It worked with Steering Committees (working groups consisting of four or five people charged with studying draft standards), a Consultative Group (created in 1981 and comprising international organisations of users of financial reports, such as IOSCO), an Advisory Council (created in 1995 to advise the Board on its choice of standards and the financing of the IASC), a Standard Committee on Interpretation (permanent committee created in 1996 with 12 members who meet to answer any questions on the interpretation of existing standards. All interpretations must be approved by the Board) and full-time technical staff.

⁹ The IASC is an independent, private organisation funded by contributions from professional accounting bodies, companies and financial institutions, accounting companies and other bodies.

¹⁰ The IFAC was set up in 1977, and is a non-governmental organisation, administered by a Council, which groups all member organisations of the IFAC. The Council elects the members of the Board and approves any changes in the statutes. The Board supervises the IFAC’s activities and selects the members of the various permanent and temporary technical committees. For more details, see the IFAC website (www.ifac.org).

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- by increasing the Trustees's oversight and interaction with parties interested by accounting standards,
- to improve the transparency of the organisation's operations by introducing new procedures and practices,
- to establish a high level advisory group of leaders of official international and regional organisations to assist the trustees in their responsibility for nominating and appointing individuals as trustees,
- to respond to concern that the experiences of those from large economies outside Europe and North America have not been represented among the Trustees by expanding the number of the Trustees from 19 to 22, with a provision for two new appointments from Asia/Oceania,
- to emphasise the need for, and to encourage extensive consultation through formal and informal mechanisms, including a reinvigorated and more effective Standards Advisory Council, and expanded liaison beyond existing due process requirements,
- to highlight the commitment of the Trustees to ensuring that an independent IASB is composed of individual that bring to its work not only technical expertise but a broad range of perspectives and skills, including practical experience,
- to take explicit note of the special needs of small and medium-sized entities.

The following geographical distribution of the Trustees must be respected at all times: 6 trustees from North America, 6 from Europe and 6 from the Asia/Oceania. The country of origin of the 4 remaining members must be such that a geographical balance is maintained. They are appointed for a 3-year mandate, which can only be renewed once, to carry out the following roles: collection of funds to finance the IASC's activities, publication of an annual report on the IASC's activities and its priorities for the coming year, appointment of the members of the IASB, IFRIC and SAC, evaluation of the strategy and efficiency of the IASC and IASB and the designation of an IASC chairman. In addition to appointing the members of the board, the trustees are also responsible for appointing the members of the *Standard Advisory Council* (SAC) which is a forum for organisations and individuals with an interest in international financial reporting.

The IASB has 14 members, 12 of whom work full-time. The main qualifications for the membership shall be professional competence and practical experience (constitution, article 19). The Trustees select members of the Board so that it will comprise a group of people representing, within that group, the best available combination of technical expertise and diversity of international business and market experience in order to the development of high quality, global accounting standards.

3.1 The conditions to international Legitimacy for the production of standards

Accounting standards contribute to the effective functioning of the economy. They are the product of efforts at standardisation by a number of national and supranational bodies. However, if we consider that accounting rules are legal standards, it is interesting to highlight that not all of these bodies are public authorities. Given the issues at stake and the potential consequences of the application of these standards, we can justifiably ask whether these bodies have legitimate authority to impose restrictive rules.

Following Tocqueville (1835) we could distinguish two kinds of democracy : representative democracy and participative democracy. A representative democracy is a form of democracy founded on the exercise of popular sovereignty by the people’s elected representatives. A participative democracy is a process emphasizing the broad involvement of constituents in the direction and operation of political systems. Participatory democracy strives to create opportunities for all members of a group to make contributions to decision-making. In the idea of deliberative democracy proposed by Habermas (1996), the equality is the right to participate to the process of decision. In a deliberative democracy legitimate lawmaking can only arise from the public deliberation of the citizen.

The legitimacy of the IASB is based on the idea of deliberative democracy. The IASB is not an expression of the public authorities, but a private organization. Its principal source of legitimacy is based on the due process who is a process of public hearing.

The above table presents the principal sources of a private organization’s legitimacy, in order to produce standards available in the general interest.

The sources of legitimacy

<u>Internal</u>	<u>External</u>
- Professionalism	- Clear mandate
- Independence	- Links with public authorities and with representatives organizations.
- Due Process	

The professionalism is important for the production of standards. The persons who produce the norms must have a high level of professionalism and technicality. The recruitment has to be done among the most competent persons. For Johnson and Salomons (1984) the institutional competence requires that the body or agency to which the authority is delegated possess a level of expertise and independence that is adequate to enable it to carry out the assigned function properly.

For the production of standards in an international level, the independence is essential. In the reality, in the case that a pressure group or a government dictates its rules, the different countries could with legitimacy refuse to apply the rules. Although, independence does not mean the denial to listen to the stakeholders, and therefor the due process is interesting.

In a Due Process all parties are informed at the time of the production of the norms. In this process the persons interested have an opportunity to have their views heard. For Johnson and Salomons (1984) ensuring all interested parties an opportunity to present their views and evidence in a reasonable and timely manner requires that they be adequately informed of matters pending before the rule-making body and be given a sufficient opportunity to provide input to the process. It requires, notice and opportunity to be heard. For this author opportunity to be heard requires that all interested parties be adequately informed of matters pending before the rule-making body and be given a reasonable opportunity to provide informational input tot the process. An other important point is the opportunity to influence the process. It requires that the final selection of rules be deferred until there has

been a reasonable opportunity for the rule-making body to consider the informational input presented by interested parties.

On the external sources of legitimacy we have the clear mandate. Indeed if a private organization gets a mandate from public bodies the legitimacy is reinforced. Especially if it is respecting the mandate and if this mandate is sufficiently clear to be able to judge. For Johnson and Salomons (1984) a clear mandate requires an assigned function that is both adequately defined and properly limited in scope and an unambiguous indication of the limits of the delegated authority.

Still concerning the external sources of legitimacy, the links with public authorities and with representatives' organizations is important. If a private organization has a private mandate from a public authority the link allows the public authorities to provide, that the mandate is duly respected, and proposals can be done.

3.2 . Application to the IASB

Professionalism

The IASC Foundation constitution indicates that the main qualifications for membership of the IASB shall be professional competence and practical experience. The Trustees shall select members of the IASB so that it will comprise a group of people representing, within that group, the best available combination of technical expertise and diversity of international business and market experience in order to contribute to the development of high quality, global accounting standards. The Trustees shall select IASB members so that the IASB as a group provides an appropriate mix of recent practical experience among auditors, preparers, users and academics.

For Wallace (1990) most of the representatives of the board enter with professional qualifications and experience in accounting and/or auditing. Many have had experience as members of national accounting regulatory boards. Many have served as President or Council members of their country's accountancy profession or as heads of the nomination organization.

Independence

The IASC Foundation constitution indicates that the selection of members of the IASB shall not be based on geographical criteria, but the Trustees shall ensure that the IASB is not dominated by any particular constituency or geographical interest.

Each full-time and part-time member of the IASB shall agree contractually to act in the public interest and to have regard to the IASB Framework deciding on and revising standards.

Members of the IASB shall be appointed for a term of up to five years, renewable once. The Trustees shall develop rules and procedures to ensure that the IASB is, and is seen to be, independent, and, in particular, on appointment, full-time members of the IASB shall sever all employment relationships with current employers and shall not hold any position giving rise to economic incentives which might call into question their independence of judgement in setting accounting standards. Secondments and any rights to return to an employer would therefore not be permitted. Part-time members of the IASB would not be expected to sever all other employment arrangements.

The independence of the IASB known criticism. Some people think that the influence of the audit industry is important (Hopwood, 1994, Wallace 2001). But we can answer that it is difficult to find good professional with no links with the audit industry.

To others, and especially to EFRAG, the European interest are not taken enough into consideration.

The due process

The IASCF has published the 19 April 2006 a “IASB Due Process Handbook”. The due Process Handbook describes the IASB’s consultative arrangements. The procedure requires that all decisions are made in public meetings and that proposals receive appropriate public scrutiny.

For the IASB the other accounting standard-setters have a role in communication the views and ideas of their constituent to the IASB threw the consultation process, providing a focus for views. Other organisations, such as representative bodies with an interest in financial reporting, may also contribute to the process.

The due process is an important point for the IASB. The objective is that all interested parties has the opportunity to express itself.

On this point , the EFRAG has the opinion that the Due Process should be drawn out (answer from EFRAG of march 10th, 2005, concerning the Constitutional revision).

All the points of view are on certain objects not always heard. For example in the first half of 2003, banks from the U.K., France and Germany lobbied against the IASB’s proposals on the mark-to-market accounting (De Lange and Howieson, 2005).

The clear mandate

The IASB has a clear mandate from the EU. The regulation n°1606/2002, of the European parliament and of the council of 19 July 2002 specify that “On june 2000, the Commission published its Communication an EU Financial Reporting Strategy : the way forward in which it was proposed that all publicly traded Community companies prepare their consolidated financial statements in accordance with one single set of accounting standards, namely International Accounting Standards (IAS), at the latest by 2005”.

European Community authorities are currently leading efforts to harmonise existing standards in this field, as part of their goal to create financial freedom within a single domestic market. Indeed, the European Council held in Lisbon on March 23 and 24, 2000, cited the establishment of a domestic financial services market as one of its main priority.

In this respect, it is important to improve the comparability of the financial reports of listed companies. Since 2001, the EC authorities have been evaluating and adopting international standards, and updating existing accounting directives in line with international practice. Clearly, the authorities are reluctant to delegate their powers to a private international body over which they have no influence (see Hopwood, 1994 for the political nature of the harmonisation debate).

European Parliament regulations and the Council of July 19, 2002 ruled that the application of international accounting standards within the European Community in order to harmonise

financial reporting is vital to ensure the markets function correctly¹¹. The idea is to impose identical standards on all sectors in order to facilitate the interpretation of financial reports (Carlson, 1997). The regulations set various conditions for the adoption of international standards, notably that they can only be applied if they are in the interests of the general public within the community¹². Community authorities therefore have the power to block the application of international accounting standards within the EC¹³, but this raises the question of whether they can actually oppose internationally accepted standards under pressure from the various Community interests at stake¹⁴. Furthermore, in a communiqué dated June 13, 2000 (“EU strategy on financial reporting: the route to follow”), the European Commission stressed that the Union should intervene as early as possible in the establishment of international accounting standards to avoid the possibility of rejection.

The Links with public authorities and with representatives organizations

The IASCF has some links with public authorities. Moreover the IASB publishes statement on its working relationships with other accounting standard-setters (February 2006). The statement identifies a range of activities that the IASB and regional and national accounting standard-setters believe they should undertake in the interests of facilitating the adoption or of convergence with International Financial Reporting Standards issued by the IASB.

The activities identified include :

- communication, both between standard setters and their constituents and among standard-setters themselves,
- project developments, including the ways in which other accounting standard-setters can assist the IASB in progressing particular projects,
- input on IASB consultative documents,
- the process and approaches other accounting standard-setters might employ in adopting or converging with IFRS's,
- co-operation in the development of interpretation of IFRS's.

In this statement of best practice, the Board emphasizes that to facilitate the communication process, the IASB should ensure that its publications are made widely on a timely basis and that its activities are regularly reported in various media. For the Board it is important that

¹¹ The main purpose of this regulation (regulation no. 1606/2002 dated July 19, 2002 of the European Parliament and the council for the application of international accounting standards) is to guarantee “a high degree of transparency and comparability in financial statements (...) and the efficient operation of the EC capital market and domestic market.” (article 1).

¹² Their application must provide a faithful and true representation of the financial health and results of a company. They must also be in the general interest of the Community and meet criteria regarding the quality of information provided to users.

¹³ This power, which is similar to a filtering mechanism, will not be a good solution if it leads to an increase in non-applicable international standards.

¹⁴ IAS 1 explicitly states that accounts cannot be deemed to have been established according to the framework of international accounting standards unless all IAS/IFRS solutions have been applied. If the European Commission does not adopt an IASB solution, we will revert to a system of Europeanised international accounting standards, which is neither the aim nor the spirit of regulation. Europe should make its influence felt upstream of the IASB decisions, and that an international accounting system where the countries decide which standards suit them is untenable.

other standard-setters use the forums on specific issues as a mechanism for encouraging their constituents to participate in the IASB's standard-setting process.

The IAS has also some links with the IOSCO. The International Organization of Securities Commissions (IOSCO) is the representative body of the world's securities markets regulators. IASB staff and IOSCO work together to resolve understanding issues and to identify areas where new standards are needed. IOSCO representative sit as observers on the Standards Advisory Council and the International Financial Reporting Committee.

To achieve a balance of professional background the IASC Foundation Constitution show that Trustees should be selected after consultation with national and international organisations of auditors (including the International Federation of Accountants), preparers, users and academics. The Trustees shall establish procedures for inviting suggestions for appointments from these relevant organisations and for allowing individuals to put forward their own names, including advertising vacant positions.

4. Concluding comments

In order to answer the question of whether a given body can legitimately establish legal standards, we first need to examine exactly how the sector is regulated. In any given sector, the professionals concerned can decide to act jointly to regulate their activities themselves (self-regulation), using contractual legal techniques or by establishing associations to formalise their regulatory function. By virtue of their statutes, these professional associations have legitimate authority to impose restrictive standards on their members, in accordance with the provisions of the law. However this system has a number of limits. On the one hand, the standards can only complete the existing law by regulating areas which it does not already cover. On the other, they can only be imposed on members of the professional association¹⁵. Consequently, these standards can only be completely harmonised at international if the applicable laws are modified. Furthermore, while professionals can use this system to define and implement regulations that serve their collective interests, these do not necessarily coincide with the interests of the majority. The State thus has a vital role to play in maintaining a balance between competition and the interests of the public, and in conciliating general and individual interests.

Another solution for involving professionals in the regulation of their sector is the professional order. These are legal entities under private law, which manage a public service. Their regulatory powers have tended to diminish with the rise of executive powers. Admittedly, orders do establish the majority of codes of compliance but they must then submit them to the public authorities for ratification. Professional orders are intended to represent their particular profession, however, the interests of that profession do not necessarily coincide with those of the general public. Consequently, a sector cannot be regulated exclusively by a professional order, or more generally by sector professionals. Orders can be used to regulate a particular profession, but an economic sector comprises more than one profession.

¹⁵ Standards may indirectly acquire a certain binding force for non-member professionals. If the professional body is deemed sufficiently representative, the judge may be tempted to resort to standards created by this body in order to assess whether the professional in question has behaved improperly in a certain situation.

For the accounting standards, this does not really pose a problem in the case of the State or international public organisations¹⁶. Literature has focused rather on the foundations for the legitimacy of regulatory authorities in the creation of legal standards and more generally for all bodies which define legal standards.

Legitimacy can be based on the assumption of political power through democratic election - the body or organisation in question derives its legitimacy from the fact that its members are appointed by representatives of the people, or from the fact that its members are elected by members of the community to which the standards will apply.

It has also been suggested that legitimacy can be derived from the procedures for establishing the standards and from the associated guarantees. We have the example of the IASB with the due process. This is based on the idea that rules are more likely to be accepted and followed if they are defined by formal procedure with the participation of those to whom they will apply. The rules thus become more credible as the procedure invites discussion and takes into account the differing interests of those concerned. Under this system, the regulatory authorities exercise their powers in accordance with the law and take different interests into account in their decisions, which are thus widely accepted. Guarantees ensure that procedures are objective and impartial, and thus inspire confidence in those to whom the decisions will apply. But for Schmidt (2002) experiences with the FASB show that an influence by specific interests groups drove the standard setting in certain cases. The due process is in fact limited.

Faced with the diversity of the public and private bodies involved in the creation of accounting rules, it seems appropriate to try and outline a system for the cooperation of public and professional authorities to ensure that public interest is more listened. Professionals have a useful role to play in the definition of accounting standards due to their practical experience and the IASB has a strong legitimacy due to his practical experience and his independence. They are better able to draw on their practical knowledge of the field to create effective and appropriate standards. But, the different states should be acting as partners in the creation of accounting standards.

The standardisation of accounting illustrates the complexity of mechanisms for creating standards in a global economic environment.

The international harmonisation of standards should not be seen in a negative light, as a weakening of the power of the State, but rather as a necessity to safeguard the interests of the majority in a global market. The State must play a sufficiently active role in the accounting harmonisation by participating in the due process of the IASB. It is important to recognise that the content of accounting standards is largely determined at supranational level and that accounting professionals play an important role.

This study confirms the pluralist nature of accounting rules as they are the product of the efforts at standardisation of a variety of bodies (private bodies, public authorities). Furthermore, accounting standards clearly show the close ties that exist between individual and general interests.

¹⁶ The State derives its legitimacy from its democratic election. Elected representatives express the will of the people and translate the interests of the majority into law. On the basis of the international treaty signed by the member States, international organisations are legitimately authorised to establish standards applicable to those members.

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