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Norm entrepreneur lobbying and persuasion: A case study involving the IASB’s modification of an exposure draft

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ABSTRACT

The dynamics of IFRS are a significant influence on regulators and accounting standard setters in many countries. Many previous studies on accounting standard setting have focused on comment letter submissions and analyzed the relationship between lobbying behavior and lobbyists’ attributes (e.g., Larson, 2008). However, how and to what extent each actor can participate effectively in the IASB’s standard-setting process has not been thoroughly studied. This case study deals with this issue and contributes to the literature by introducing the theoretical perspective of norm entrepreneur actions during accounting standard setting. It investigates a case involving the modification of an IFRS exposure draft that did not reflect Japanese opinions. This study identifies two factors that appear to be crucial in relation to the IASB’s final decision: the actions of Japanese norm entrepreneurs and their analogical persuasion.

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1. Introduction

As more than 130 jurisdictions already either require or permit the use of International Financial Reporting Standards (IFRS) (Pacter, 2016), the dynamics of IFRS have a significant influence on regulators and accounting standard setters in many countries. Thus, a national accounting standard setter’s previous experience in terms of securing political support for domestic standard-setting processes may no longer be relevant (Richardson & Eberlein, 2011). Rather, each country’s accounting standard setter must not only consider their domestic accounting regulations but also participate effectively in establishing IFRS by conveying national concerns to the International Accounting Standards Board (IASB). In other words, with the global diffusion of IFRS, issues in accounting standard setting have become a matter of international politics. Power (2009) states that the setting of accounting standards is inevitably political, especially when done globally. Under such circumstances, each national accounting standard setter needs to exercise diplomatic skill in the political process of global accounting standard setting.

For example, concern has been expressed in Japan, where in June 2013, the Keidanren (Japan Business Federation) expressed the following opinion: “In terms of consideration of IFRS, Japan should continue to express ‘All Japan’s opinions through the Accounting Standards Board of Japan (ASBJ) and other channels so that Japan’s opinions will be sufficiently reflected” (Keidanren, 2013, p. 6). In addition, the Business Accounting Council (BAC), an advisory body to the Financial Services Agency of Japan, published their Present Policy on the Application of International Financial Reporting Standards (IFRS). It argued that “while there have been various moves around the world to achieve the global objective of a single set of high-quality global accounting standards, the next few years are an important time for Japan from the viewpoint of how Japan should become involved in this formulation” (BAC, 2013).1

These responses reflect each accounting standard setter’s awareness of the significance of political activity in the context of global accounting standard setting. However, how each accounting standard setter can effectively communicate its concern to the IASB has not been fully studied. Therefore, how the IASB can be persuaded to accept national accounting norms is an important research subject in this era of IFRS.

To tackle this subject, this study examines the political significance of national interests in the process of international accounting standard setting and investigates how specific actors attempt to protect their interests (traditional accounting norms).

1 In another example, the Korea Accounting Standards Board (KASB) and Financial Supervisory Service stated in a joint report that “now that Korea is asked to get involved more proactively with and play a more important role in the IFRS-setting process, having vigorous interaction with constituents, local and global, has become even more crucial for Korea as it will lay the foundation upon which Korea can build in the future” (KASB and FSS, 2012, pp. 36–37).
Therefore, this study focuses on a change in a specific accounting treatment (of dividends received) from the exposure draft to the final standard released as part of the IFRS and identifies factors that contributed to the change through a theoretical lens of diffusion of norms. As international politics in relation to global standard setting is so complicated, a systematic perspective developed by Finnemore and Sikkink (1998) that captures the dynamism of international norms (i.e., the life cycle of norms) is used as the theoretical basis of this study. Their study is classified as one of the constructivist normative studies, and their perspective was applied to an international comparison of environmental reporting practices (Bebbington, Kirk, & Larrinaga, 2007). The framework of Finnemore and Sikkink (1998) is used in this study because it considers different levels of agreement in relation to norms. Finnemore and Sikkink (1998) treat these differences as continuous and argue that the dynamics of the agreement process can be examined from the perspective of the “life cycle (diffusion stages)” of norms (Finnemore & Sikkink, 1998, p. 892). This perspective is useful when considering the main focus of this study, namely, the dynamics of how local accounting norms are diffused to the IFRS. In particular, they focus on a tipping point at which agreement is reached among a critical mass of actors in relation to an emergent norm (Finnemore & Sikkink, 1998, p. 892). In the present study, the main focus is the tipping point at which a local emergent accounting norm is accepted by an authoritative international organization such as the IASB.

Currently, a set of IFRS can be formally, if not substantially, regarded as comprising international rather than national accounting norms. However, many international accounting norms begin domestically and become international through the efforts of various norm entrepreneurs. Norms do not appear from nowhere; they are actively created by norm entrepreneurs who have strong notions about what is appropriate or desirable behavior in their community (Finnemore & Sikkink, 1998). Norm entrepreneurs are leading individuals or organizations who make an effort to diffuse specific types of norms. In the process of diffusing international accounting norms, they are likely to conflict with domestic regulations and standards, which can produce important variations in compliance with and interpretation of these norms (Finnemore & Sikkink, 1998). Therefore, how they can best be diffused and what kinds of factors can accelerate the process is the focus of this study.

Based on the theoretical perspective mentioned above, this study considers the process of setting IFRS 9: Financial Instruments. The aim of the standard was to simplify accounting standards for financial instruments by revising the previous standard (IAS 39) in response to the financial crisis (Yamada, 2013, p. 335). IFRS 9 requires an entity to classify financial assets as subsequently measured at amortized cost or fair value based on the entity’s business model for managing financial assets. An entity assesses whether its financial assets meet the condition based on the business model objective determined by the entity’s key management personnel (IASB, 2009b, para. B41). During the standard-setting process, the IASB changed the classification of dividends from strategic equity investments that had been included in the exposure draft in response to strong opposition by various parties. This study considers this change by analyzing the comment letters that were submitted, discourses of powerful actors, and information obtained from an interview with a former IASB member. From the perspective of international norm diffusion, the study highlights two crucial factors, norm entrepreneurs’ actions and their effective analogical persuasion, that might have contributed to the changes to the exposure draft.

The rest of the paper is structured as follows. First, the extant literature on accounting standard setting is reviewed, two divergent views of global accounting standard setting are compared, and then the theoretical perspective underlying the study is presented. Second, an insight from international politics is considered and applied to the dynamics of global accounting standards. Third, the scope and methodology of the study are outlined. Fourth, the process that led to IFRS 9 is investigated. Based on this investigation, it is found that the existence of active norm entrepreneurs was effective in achieving a modification of IFRS 9. Then, based on an interview with a former IASB member, I confirm that logical persuasion using analogical argument is likely to be accepted by IASB members. Finally, conclusions and future research opportunities are presented.

2. Technical and political viewpoints in relation to global accounting standard setting

Most people acknowledge that the global spread of IFRS has been significant in recent years. Global accounting standard setting can be theoretically explained from either a technical or a political viewpoint. The technical view sees standard setting essentially as “identifying the best accounting practice for a particular issue” (Larson, 2007, p. 214), and tends to emphasize the economic consequences of accounting standard setting. For example, Barth (2008) argues that globally unified accounting standards would decrease three types of related costs. First, they would decrease the costs global firms incur in preparing and auditing their financial statements. Second, they would decrease the costs financial statement users incur in interpreting corporate financial statements issued in various countries around the world. Third, these benefits would probably lead to a decrease in the cost of capital for global firms. Indeed, the EU previously justified the widespread adoption of international accounting standards on the grounds of lower costs and improved economic rationality (Rodrigues & Craig, 2007).

However, it remains unclear whether the IASB clearly recognizes the future costs and benefits of its standards. Several studies have adopted a skeptical viewpoint in relation to identifying the obvious benefits of a single set of global accounting standards. For instance, Eccher and Healy (2000) focused on several differences among countries and implied that global accounting standards were not optimal. In other words, simply assuming that the IFRS is relevant to all societies ignores the institutional differences between nations in terms of infrastructure, culture, legal requirements, and political systems (Chand & White, 2006), Zeff (2007), also doubted whether convergence of accounting standards would enhance comparability because of the cultural differences (including those relating to business, finance, accounting, auditing, and regulatory practices) among countries. Based on environmental determinism theory, Rodrigues and Craig (2007) described differences in tradition, history, religion, and culture among countries and the effects of these differences on opinions, rules, and business accountability, which are not sensibly reflected in harmonized accounting standards. Similarly, Leuz (2010) and Toker (2005), argued that true convergence in reporting practices is not yet within reach, and would require a much broader convergence of countries’ institutional frameworks, which was seen as costly and unrealistic in the near future (and probably not even desirable). Chua and Taylor (2008, p. 467) stated that “while the importance of compa-
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