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The rise and rise of IFRS: An examination of IFRS diffusion

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ABSTRACT

We seek to understand the ever-increasing push towards the international harmonization of accounting standards and particularly the inexorable rise of standards produced by the International Accounting Standards Board (IASB). While the primary justifications for the increasing recognition given to these standards (IFRS) are economic, we question whether the empirical evidence to date has yielded convincing support for these arguments. We therefore offer an alternative explanation for the origin and diffusion of IFRS that incorporates social and political factors. Outsourcing the manufacture of accounting standards to a single private agency appears to be a rational, lower cost option – lowering both economic and political costs for individual states as long as they continue to retain residual decision rights with respect to the adoption of IFRS. However, such outsourcing must also be perceived to be legitimate. IFRS confer institutionalized legitimacy because they possess three characteristics required of a technology for global governance. These are sponsorship by powerful interest groups/regulators, internationality and plasticity. We therefore conclude that the widespread diffusion today of IFRS can at best be only partially explained as an economically rational phenomenon. Rather, the demand for legitimate action in the face of tightly coupled and complex global markets is at least equally important in generating support for IFRS.

> Full harmonization of international accounting standards is probably neither practical nor truly valuable (Goeltz, 1991, p. 85).

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1. Introduction

Nearly two decades ago, views such as those expressed by Goeltz would not have been uncommon. However, the rapid rate at which accounting standards issued by the International Accounting Standards Board (i.e., IFRS) have become the default standards in many countries shows no sign of slowing.[1] Indeed, the recent decision by the United States Securities and Exchange Commission (SEC) to allow foreign registrants reporting under IFRS to avoid providing reconciliation with US GAAP seems likely to add to the speed with which the IASB standards will ultimately become the default standards for domestic US firms as well.[2] Of course, US GAAP and IASB standards could somehow co-exist over an extended period and even provide a degree of competition in terms of alternative sets of accounting standards. However, we doubt that this will occur, even if there is some logical support for a degree of competitive tension in the standard setting process (Sunder, 2002; Jamal and Sunder, 2007).[3] Although some have argued that a decision by the SEC allowing domestic registrants the possibility of choosing between reporting under US GAAP or IFRS may actually slow the process of convergence (Street and Lithicum, 2007), we argue that the march towards a single set of standards (i.e., IFRS) issued by a single, international standard setter (i.e., the IASB) will continue to gather pace.

Given the seemingly inexorable and irreversible rise of IFRS as the global accounting benchmark, it is timely to ask how this has occurred. We argue that, for the most part, the rationales offered publicly supporting the rise of IFRS are economic ones. However, even a brief review of extant evidence suggests that substantive empirical support is not as strong as some may assume (or perhaps want to assume). This leads us to argue that rationales which incorporate a broader social and political perspective will be useful in understanding the inexorable rise of the IASB as a global accounting standard setter. Put simply, we argue that the move towards a single set of standards under the auspices of a private sector international issuing organization independent of state-sponsored national bodies is as much, if not more about the politics of setting accounting standards. The development and diffusion of IFRS is more about political and social dimensions of globalization than it is about the alleged economic benefits of convergence in international accounting standards.

We commence our analysis by briefly reviewing the economic rationales offered for convergence towards an internationally accepted set of accounting standards. Three key reasons stand out. These are transparency, quality and comparability. On the first point (transparency) we note that periodic financial statements are just one component of the information set used to evaluate the performance of publicly traded firms, a point recognized in the seminal work of Ball and Brown (1968), but somewhat ignored since. Indeed, we expect that the most important source of demand for financial reporting is found in the contracting role of accounting, rather than as a primary means of investment evaluation by external investors (Watts and Zimmerman, 1986).

With respect to the second popular rationale (improved quality) we note that extant empirical evidence suggests that the quality of the financial reporting process has more to do with the way in which standards are enforced than variation in the standards themselves. It is also difficult to design powerful tests of the effect of a change in accounting standards if the change is not mandatory. Further, there are many different empirical constructs for accounting quality, which frequently yield conflicting results.

Finally, on the third point (comparability), we are struck by the almost complete lack of evidence to support the view that results reported under different accounting regimes lack comparability. It appears as though most, if not all empirical research on this point focuses on the comparability of other properties (e.g., value relevance, and conservatism) rather than attempting to define and measure comparability per se. This point has only been recently recognized among researchers interested in empirically documenting properties of published accounting numbers (DeFranco et al., 2007).

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[1] Throughout the paper we use the consistent terminology IFRS to refer to standards issues by the IASB and its predecessor, the IASC.

[2] See http://www.sec.gov/rules/final/2007/33-8879.pdf.

[3] As we interested in reviewing rationales offered for harmonization, we do not consider further the possible role of competitive tension between standard setting agencies. The pro-harmonization arguments are typically premised on a single set of standards, rather than competition among standard setters.

Our (brief) review of extant empirical evidence calls us to question just how much support there is for convergence to a single set of international accounting standards, at least in the way that supporters of IFRS typically claim. So why has so much attention and effort been given towards achieving this? We doubt that the answer lies in the economic role of accounting, but rather the political nature of accounting standard setting. To that end, we note that the crucial impetus at a national level for adopting IFRS has typically been from the government and/or government agencies.

We also note the way in which standard setting at the national level has been fraught with political debate in prior years. In other words, transferring the accounting standard setting process to an organization outside national boundaries may be a means of eliminating what many in the regulatory and political setting may see as a "messy" process at the national level. If publicly available accounting information is but a small part of the total information set that influences resource allocation in capital markets, there is an incentive for regulators not to make costly specific investments in its governance.

Our review of the evidence is admittedly selective. However, at the same time, we are struck by the lack of empirical evidence that clearly supports the economic rationales typically offered for the move towards a single set of standards. While that does not disprove these rationales, it does surely raise questions. We believe there is an opportunity for research, especially where new methods can be identified for either directly testing the claims made in support of convergence, or alternately the development of measures that can better separate the political and economic rationales.

The remainder of the paper proceeds in the following manner. In Section 2 we briefly review the three key arguments in support of convergence that are typically offered, and consider whether extant empirical evidence yields support. In Section 3 we briefly consider the political nature of the accounting standard-setting process, and outline what we term a political rationale for convergence (Hopwood, 1994). Section 4 concludes.

2. Economic rationales – a brief review of the evidence

2.1. IFRS as timely information for investors?

The idea that a single set of accounting standards would provide an important aid for external investors to evaluate the performance of companies across national boundaries is well established. Long standing prevailing arrangements such as the US requirement for foreign registrants to provide a detailed reconciliation with US GAAP (i.e., 20-F forms) is an obvious example of the view that it is essential for investors to have a set of financial statements in their own "language" (i.e., prepared under standards with which they are most familiar).[4] However, there are at least two sets of empirical findings that call into question just how useful and/or important such practices really are.

First, since Ball and Brown (1968), it is evident that external financial reports, while in some senses "value relevant", are not especially timely sources of information. This is hardly surprising, as stock prices change in response to new information, but periodic financial statements provide a summary of past transactions. Hence, studies that examine the responsiveness of stock prices around the release of periodic financial statements typically display a low level of explanatory power (Kothari, 2001). In other words, it cannot be claimed that periodic financial statements cause stock price changes, except to a very small extent. Investors likely rely on the myriad of other information sources, including analysts reports, media coverage and ad-hoc disclosures made by the firms themselves.

Indeed, it seems to us that the role of Ball and Brown (1968) in demonstrating what is commonly interpreted as the value relevance of financial reports (particularly earnings) has resulted in an overstatement of how important earnings information is as a source of timely (i.e., new) information. For example, Francis et al. (2002) document what they characterize as an increasing usefulness of quarterly earnings announcements for a large sample of US firm-quarters over the period 1980–1999. While their characterization of usefulness is measured as the extent of market reaction per unit of

[4] Whether 20-F reconciliations actually serve as a significant source of information for investors is a function not just of the apparent "value relevance" of the reconciling amounts, but also their materiality and the specific transactions for which the two systems yield different results (Venkatachalam, 1999).

unexpected earnings, it is worth noting that only a very small proportion of the abnormal stock return at the time of an earnings announcement can be explained by a measure of "earnings news".[5]

More recently, explicit recognition of this point is provided by Ball and Shivakumar (2008). They capture the relative importance of earnings announcements in providing new information to the share market via the *r*-squared from a regression of calendar year stock returns on their four quarterly announcement date stock returns. Using a large sample of US firm-quarters (years) from 1972–2006, Ball and Shivakumar show that around 9% of the total annual information is explained by the four quarterly earnings releases. Hence, on a quarterly basis, around 1–2% of annual information is explained by each quarterly release.[6]

So what is the economic role of periodic financial statements, especially key summary measures such as earnings? Given the lack of timeliness, Ball and Shivakumar (2008) argue it is logical to conclude that the primary role of financial statements is the monitoring and settling up of contractual relationships (Watts and Zimmerman, 1986), as well as providing a means of disciplining prior expectations (Gigler and Hemmer, 2001). Examples of a contractual role for accounting that are well established via prior research include debt contracting and the monitoring and rewarding of management.

The pre-eminence of a contracting role for financial statements has important implications for advocates of international harmonization of accounting standards, and ultimately, a single global set of standards. Is there justification via means of similar contractual design and implementation across countries for having similar accounting standards? At one level, the answer is clearly yes, via the conduct of business by global corporations. These organizations borrow internationally, and also implement global compensation arrangements. There are obvious savings in having a single set of accounting standards. But what of firms that are national rather than global? If national boundaries define in at least some ways variation in debt contracting conventions, then there are likely to be costs imposed on the contracting parties if mandatory accounting changes occur in the name of harmonization. Of course, this does not mean that such changes will not be value enhancing for some firms. Kim et al. (2007) show that a sample of non-US borrowers who voluntarily switch to international accounting standards experience lower borrowing costs, but presumably firms that can benefit will do so, and those that do not receive such a benefit will not want to change.

A similar point can be made with respect to the role of financial reporting in evaluating managerial performance. Wu and Zhang (2008) identify a group of continental European firms that voluntarily adopt either IFRS or US GAAP between 1988 and 2004.[7] They find that these firms display a higher level of sensitivity of both CEO turnover and employee layoffs to accounting earnings after the change in accounting method. Once again, the evidence is consistent with a non-share market demand for accounting information being the pre-eminent determinant of what is most suitable. Anecdotal evidence, in the form of the decision by Daimler-Benz to switch from German to US GAAP in 1996 and its justification of that decision (Ball, 2001) also points to the contracting role of accounting as a critical determinant of how accounting standards have evolved at a national level, and presumably why they differ between countries.

2.2. *Better quality accounting?*

Irrespective of whether the primary role of financial reports is as a timely source of new information for external investors or as a means of monitoring and enforcing contractual relationships, there is still an overriding concern with financial reporting quality. One frequent justification then

[5] Based on Table 7 of Francis et al. (2002), it appears that unexpected earnings explains, on average, around 2% of the variation in risk-adjusted stock returns centred on the earnings release date.

[6] Further evidence of the relatively low importance of earnings announcements as a timely source of new information is found by examining trading volume. Ball and Shivakumar (2008) show that, on average, quarterly earnings announcements are associated with around 0.25% of annual trading volume.

[7] The fact that Wu and Zhang (2008) treat adoption of either IFRS or US GAAP as a move to "international" standards is a further issue that we do not consider here.

for IFRS that is applicable from either perspective is that international harmonization will result in higher quality financial reporting. However, while there are several studies that examine the quality of financial reporting after the adoption of IFRS, the results are somewhat mixed. Moreover, there are many different empirical constructs, some of which reflect attributes of the accounting numbers themselves (e.g., accrual based measures of manipulation) and some of which reflect the interaction between accounting information and capital markets (e.g., measures of value relevance).[8] In addition, there is the issue of whether adoption of IFRS (or for that matter US GAAP) is voluntary or mandatory.

Most studies on the effect of voluntary adoption of IFRS focus on capital market effects (e.g., cost of equity capital or measures of liquidity), on attributes of analysts forecasts (e.g., dispersion and accuracy) or on the extent of institutional ownership.[9] In reviewing such studies, Leuz and Wysocki (2008) characterize the findings as mixed. This extends to studies that examine value relevance via the association with stock returns and/or stock prices. For example, Barth et al. (2008) examine a sample of firms from 21 countries that voluntarily adopted IAS between 1994 and 2003. They find that accounting numbers reported by these firms demonstrate greater value relevance than for a matched sample of firms selected on the basis of country, firm size and time period. However, this effect is not as strong when the voluntary adopters are used as their own control (i.e., comparing the pre-and post-adoption periods). Further, there is no discernable difference between the change in value relevance experienced by the voluntary adopters and that experienced by the control firms. Similar conclusions apply to other measures of accounting quality also examined by Barth et al. (2008).

Studies which examine attributes of accounting quality for voluntary adopters of IAS face the problem of controlling for the incentives which led that set of firms to select IFRS (or US GAAP in some cases, such as in Leuz and Verrecchia (2000)). Ideally, an evaluation of the claim that IFRS (or similar) results in higher accounting quality would examine instances where a mandatory switch occurred. One such example is Daske et al. (2007), who examine the effect of IFRS adoption in 26 countries. They measure market liquidity, cost of equity and Tobin's Q. While they find some evidence of improvements, what is especially noticeable is that the improvements are restricted to countries where there are already institutional arrangements that provide strong incentives for high quality financial reporting, as well as a relatively robust regulatory regime. In reviewing the evidence, Leuz and Wysocki (2008) conclude that firms' reporting incentives and regulatory regimes are a critical component of overall accounting quality. What they are unable to divine is the extent to which accounting quality effects are incremental to a set of mandatory standards, as distinct from the institutional and regulatory environment.

Overall, evidence on the question of whether IFRS (or even US GAAP as a rival) leads to higher quality financial reporting, let alone actual economic benefits to owners, is unclear. Most evidence is based on voluntary adoption of accounting standards, and this is fraught with problems in separating the incentive effects associated with voluntary adoption. On the other hand, the limited number of studies examining the effect of mandatory IFRS adoption suggest that most, if not all significant differences are attributable to institutional and regulatory factors that differ across countries. The lessons from extant research seem reasonably clear.

2.3. Comparability – what is it?

We are struck by the extent to which advocates of harmonization of accounting standards focus on comparability as a desirable property of financial reporting. One recent commentary (Tarca, 2008) puts the issue succinctly: "the aim of adoption of IAS/IFRS in Australia was to improve the international comparability of Australian companies financial reporting". This type of sentiment is not atypical. However, the precise meaning of comparability is not typically explained, and prior empirical studies tend to define comparability as meaning a similar set of "other" accounting properties. Hence, different countries are said to have comparable financial reporting if financial reporting in those

[8] Schipper and Vincent (2003) provide a detailed discussion of alternative constructs of accounting quality.

[9] We do not summarise individual studies of this type. A detailed summary can be found in Leuz and Wysocki (2008).

countries demonstrates similar levels of value relevance, conservatism, earnings management and so on (Ball et al., 2000).[10] However, we doubt that this what accounting standard setters have in mind when they argue that comparability is a desirable attribute of financial reporting.

DeFranco et al. (2007) note that the accounting literature lacks an empirical measure of financial reporting comparability. As a result the importance of comparability as such is not established empirically. This likely reflects the failure of prior academic research to construct an empirically tractable measure of comparability. They suggest that the ability of other firms' earnings to predict the respective firm's earnings provides a measure of comparability (i.e., the likelihood that similar firms display a high level of earnings covariance). Having established a measure of comparability, DeFranco et al. then show that this attribute of accounting has some value, using properties of analysts' forecasts as a measure of the effect of comparability. They show that earnings comparability is positively associated with analysts' forecast accuracy and negatively associated with analysts' forecast bias.

An obvious question then is whether the international harmonization of accounting standards results in greater comparability. We are unaware of any studies that apply the insights from DeFranco et al. (2007) at a cross-country level, but this seems a very obvious research opportunity. Likewise, to the extent that existing IFRS and US GAAP can be seen as competing financial reporting systems, tests of the type outlined by DeFranco et al. would shed light on the extent to which comparability differs between the two sets of standards. In short, while the importance of comparability as an attribute of financial reporting is frequently a key justification for international harmonization, we have no rigorous empirical evidence on this point.

3. The politics of global governance

3.1. The development of IFRS

In 1994, Hopwood wrote the following:

> "…..our understanding of many key aspects of international accounting is more rudimentary than many people think and than some would want us to believe. The processes of institutionalization in the area are poorly understood. The emergence of interests in international accounting has not been explored. Little is known to outsiders of the complex and shifting politics that pervade the area".

Nearly two decades later, these sentiments continue to resonate. We have already noted that extant evidence does not provide strong justification for frequently cited economic benefits that are said to arise from global harmonization and regulation of financial reporting practices. So why has disclosure and reporting regulation been so pervasive in advanced economies (Leuz and Wysocki, 2008)? More specifically for the purpose of this paper, why have governments been persuaded and increasingly moved to adopt IFRS either as complete or incomplete sets (see Nobes and Zeff (forthcoming) for a discussion of various types of adoption), thereby outsourcing the regulation and standardization of financial reporting to a distant, professionalized, private sector agency? Our focus is to investigate this second question and identify some possible reasons for the structural origins and rapid diffusion of IFRS.

The adoption of IFRS has been particularly noticeable in the last two decades. This period is also said to characterize increased globalization and integration of business and capital markets. As proponents of harmonization like to point out, business today is global. But what does globality mean? Scholte (2002) points out that globality has at least four interrelated aspects: internationality, liberality, universality and supraterritoriality.

Internationality refers to the increased volume, complexity and frequency of cross-border interaction in goods, services and people. For example, in terms of cross-border financial flows, the world

[10] A recent example of this tendency is Bueselinck et al. (2007). They initially define reporting comparability as "the ability of earnings to account similarly for alike transactions", but then conjecture that such comparability is "largely affected by the way the accruals system recognizes losses in a timely fashion or smooths income over distinct periods". In other words, comparability is tested by comparing the extent of conditional conservatism and income smoothing.

total of bank deposits owned by non-residents of a given country had risen from $20 billion in 1964 to $9600 billion in 2001 and outstanding balances on syndicated international commercial bank loans had increased under $200 billion in the early 1970s to well over $8000 billion in 2001 (BIS, 2001). Liberality arises because of the relative low level of statutory barriers to cross-border flows in the form of tariffs, foreign exchange regulations, capital controls, visa requirements. Universality prevails when modes of practice, symbolic objects and experiences are diffused to many parts of the globe – from Arabic numerals, to McDonald hamburgers, to Chanel perfumes. Finally, supraterritoriality points to the ability of forces such as climate change and telecommunications to connect people in ways that largely transcend territorial geography. Such connectivity and interdependence exists with little regard to fixed territorial spaces, borders and physical distances.

What are some of the consequences of globality? One answer is that increased globality demands global governance in order to achieve a socially desirable level of disclosure (Tweedie and Seidenstein, 2005). From time immemorial, markets have emerged as co-ordination mechanisms for the social production of goods and services. In situations of market failure, governments have been traditional regulators. However, the focus of governments was on regulating affairs within defined territorial borders.

With increasing globality, the question of governing activities and enterprises has required that governments collaborate not only on a localized regional basis (such as the European Union, ASEAN, etc) but on a larger basis (for example, the United Nations and its associated agencies). The emergence of numerous intergovernmental agencies is a well-documented phenomenon of the late nineteenth century and early 20th century. The oldest examples of such agencies are the International Telecommunications Union and the Universal Postal Union, both formed in the late 1800s. Held and McGrew (2002) point out that at the beginning of the twentieth century there were just 37 intergovernmental organizations whereas in 1996 there were 1,830 intergovernmental organizations.

With respect to the governance of finance and capital markets, we have seen over the last century the emergence of networks of civil servants that are now increasingly institutionalized as separate permanent bodies (see Scholte (2002) for a more detailed discussion). For example, under the auspices of the Organization for Economic Cooperation and Development (OECD), transgovernmental groups of civil servants have met to formulate rules with respect of financial liberalization, cross-border taxation, and so on. The Bank for International Settlements, for example, dates back to 1930 and its membership consists of 45 national central banks. Similarly, the International Organization of Securities Commissions (IOSCO) was created as an inter-American body in 1974 but now involves nearly a hundred national securities authorities. Further, the International Association of Insurance Supervisors (IAIS) was formed in 1994 and has quickly grown to link regulators in over a hundred countries. Since 1996, these two bodies (IOSCO and IAIS), together with the Basel Committee on Banking Supervision (formed as a standing committee of the G10 in 1975), are part of a Joint Forum on Financial Conglomerates that seeks to promote cooperation between banking, securities and insurance supervisors.

It could be argued that the globalization of business has required that global standards be developed; and that these would by necessity be beyond the jurisdiction of a single government agency. As indicated earlier, if these were indeed the economic drivers for the rise of IFRS, the evidence to date does not support this thesis strongly. But putting these economic rationales aside, there remains the question of the structural form of a single standard-setting agency. Conceivably, an intergovernmental agency could have become involved in the setting of global accounting standards. Given the existence of other intergovernmental agencies such as IOSCO, exemplars of such modes of intergovernmental collaboration were readily available. The point we are making is not that such an alternative arrangement would have been more efficient. Rather, the point is that, in principle, there could have been a different arrangement that involved a single intergovernmental standard-setting agency. So, why did this not eventuate?

This question is all the more interesting as by the mid-1990s there were several intergovernmental groups working specifically in the area of accounting, for example, the OECD Working Group on Accounting Standards, the UN Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting, and the European Union's Accounting Advisory Forum. Why were none of these seen as possible agencies for the development of international accounting standards? To date, researchers have not explored this question.

One explanatory factor could be the historical institutionalization of accounting standard-setting within national agencies sponsored by local accounting professional associations. Fearful of direct government control, accounting associations, especially the earlier Anglo-Saxon associations, have sought and fought for self-regulation since their inception in the late 1880s. Reflecting this focus on self-regulation, accounting standard-setting in certain Anglo-Saxon countries, such as Australia and the UK, was controlled by bodies sponsored by local professional associations. For example, in Australia, the Australian Accounting Standards Committee was originally sponsored by CPA Australia and the Institute of Chartered Accountants in Australia. Control was therefore always private as opposed to public.

Hopwood (1994) further suggests that the desire of accounting associations (and just as importantly, the accounting and audit industry), to maintain professional control over international standard setting was key to the transformation of the IASC (see also Camfferman and Zeff (2007) for a history of the IASC). The IASC had started life as an advocate for the British audit industry prior to Britain's entry to the European Union. Over time, this "Britishness" was erased such that the IASC came to be seen to as an "international" body that was politically not aligned. Hopwood argues that it was the US Securities and Exchange Commission (SEC), acting through the committees of IOSCO, which successfully "pushed" the IASC to construct an international basis for accounting disclosures that would be acceptable to the USA, and indeed to a wider international community because of its non-American origins. But the question remains, why was an intergovernmental agency not seen as a politically acceptable and rational arrangement? Why did the SEC and IOSCO push the IASC, if indeed it did? Why was this seen as the best option at that time?

Is there any evidence to support Hopwood's hypothesis? Interestingly, since its publication in 1994, there has been no subsequent study that specifically seeks to test Hopwood's claims. At this point, it simply remains a plausible thesis. While the globalization of business might have created a rational economic demand for a technology of global governance (in the form of IFRS), the supply of these standards through a private as opposed to public agency may be largely a political exercise engineered (at least in part) by a coalition of powerful interest groups which included regulators and a globalizing accounting and audit industry.

3.2. *The diffusion of IFRS*

The desire by the Anglo-American accounting and audit industry to retain control over the international accounting standard-setting process might explain how a private sector organization (i.e., the IASB) came to own this process. However, we know little about why countries have increasingly moved to adopt IFRS in preference to their local accounting standards and, indeed, in preference to US GAAP. Nor indeed, do we understand the varieties of adoption that currently exist. As Nobes and Zeff (forthcoming) point out, some countries such as Israel and South Africa have already legislated to accept IFRS without change while the European Parliament has decided to endorse and in that sense adopt only a subset of standards deemed more appropriate to its needs and concerns. Indeed, instead of using the term adoption, it might be more appropriate to use the term translation (see Latour (1987)) to highlight the varieties of adoption that already exist.

In seeking to understand diffusion, a mixture of politics and economics appears to offer elusive answers. "Crises" on a regional scale which affect tightly coupled globalised capital markets appear to be one catalyst for diffusion. The IASB (2003) writes that the Asian economic and financial crisis in 1997/1998 "showed the need for reliable and transparent accounting and financial reporting to support sound decision-making by investors, lenders and regulatory authorities". It is unclear whether the adoption of a harmonized/standardized set of accounting standards would have averted the 1997 crisis. Indeed, evidence in Ball et al. (2003) explicitly questions whether common accounting standards will over-ride the effects of local institutional factors. Despite the similarity of the accounting standards across the four countries examined in their study (Hong Kong, Malaysia, Singapore and Thailand), they found that the properties of reported earnings differ in line with country-specific institutional factors.

But perhaps, over a decade ago, in the face of a major currency crisis and in the absence of strong evidence to the contrary, the functional political response was to act as though substantial financial crises could be satisfactorily managed through constructing an object called international best accounting practice. Power (2007) notes that a stream of apparent financial disasters and scandals, from the collapse of Barings Bank to the near bankruptcy of particular nations, has challenged and threatened the capacities of globalised institutions to organize and act in the face of uncertainty. Power argues (p. 5) that these events suggest "a world which is out of control, where failure may be endemic, and in which organizational interdependencies are so intricate that no single locus of control has a grasp of them". Power also quotes approvingly from Douglas and Wildavsky (1982, p. 1): "Can we know the risks we face, now or in the future? No, we cannot: but yes, we must act as if we do". Crises require action even though actors might not be certain that the solution offered is efficacious and deliver the benefits assumed.

As the IASB (2003) document further notes, it was the finance ministers and central bank governors of the G7 countries who pressed for the development of international accounting standards and who called on countries to adopt them. In addition, Graham and Neu (2003) note that when the International Monetary Fund put forward its large rescue package for Indonesia, they required that the country should revise its financial system regulations to incorporate international best practice. In short, suprastate agencies appear to have played a major role in requiring that nations perceived to possess weaker forms of financial governance and surveillance adopt standards that are seen to possess an internationally recognized level of quality and hence legitimacy.

The role of suprastate agencies in the diffusion of IFRS is clearly evident in the 2002 decision of the European Union to require that approximately 7000 listed companies in its member states report using IFRS (that were endorsed) from 2005 onwards. Was this decision connected in some ways to the earlier activities of suprastate agencies in the management of the Asian currency crisis? Future research might throw some light on the rationales for the EU decision. Clearly, it was a decision that gave considerable legitimacy to IFRS.

Institutional theorists suggest that once powerful first movers act to adopt/endorse particular types of behaviour, these can come to be regarded as the field norm and others follow suit because adoption or mimicry confers social legitimacy within that field of action. Typically, institutional theorists (DiMaggio and Powell, 1983; Meyer and Rowan, 1977; Scott, 1987) have been keen to examine how isomorphism arises in organizational fields. Three forms of isomorphism have been identified. These are coercive (standardization brought about by the rule of law, etc.), mimetic (standardization through efficient, copying behaviour after powerful first movers act) and normative (standardization brought about by authoritative agencies such as professional associations and accreditation agencies).

In a study of the adoption of generally accepted accounting principles by US state governments, Carpenter and Feroz (2001) argue that legitimacy concerns were important reasons for their adoption. Much earlier, Tolbert and Zucker (1983) had studied the diffusion of civil service reform in a sample of cities and found that early adoptions were influenced by city requirements but later adoption was influenced by institutionalized definitions of legitimate structural form. Diffusion was also quicker when required by law. If institutional theory were to explain government/state action in a field of states, it could be used to explain the diffusion of IFRS post the Asian currency crisis. That is, as powerful groups such as the World Bank, the International Monetary Fund and the European Union come to accept IFRS as a legitimate form of international best practice, later adopters will adopt in order to secure legitimacy.[11] Research could test such a hypothesis.

Research might further investigate how and why did IRFS appeal as international best accounting practice? Clearly, in order to appeal internationally, a technology of global governance must somehow embrace diversity. How was internationality constructed given the British origins of the IASC? As Hopwood (1994) has suggested, internationality importantly came to be defined as "not-American". Politically, it would have been difficult for US GAAP to have been seen as international standards since they were so clearly identified with the aims and agendas of the SEC. This is despite the actions of individual companies with individual reasons for using US GAAP (see Zeff (2002)). IFRS may therefore be perceived as more international simply because they are not American. Nevertheless, it is important to

[11] Incidentally, actions to secure legitimacy should not be construed as "irrational". Earlier institutional work tended to juxtapose means-end rationality with legitimacy and as Greenwood et al. (2008) point out, later work has criticised such arguments.

note that even with IFRS, its claim to internationality is an imagined, and possibly manufactured property.

Internationality connotes many dimensions. One of these is that the standard is not closely aligned with the economic or political institutions of any particular nation; that it is independent of political allegiances. However, IFRS are clearly grounded in a strong emphasis on investor protection, and within a particular mix of regulatory mechanisms and institutionalized governance technologies. As a consequence, their effectiveness depends on the operation of particular (mainly Western) social, legal and political institutions. In the presence of other institutional frameworks, effective harmonization is likely to be more variable.

Finally, drawing upon actor network theory (Latour, 1987), it could be argued that IRFS has diffused quickly partly because it is a principles-based set of rules that enables local customization and local translation. By comparison, US GAAP is seen as a more tightly specified set of rules and this lack of plasticity makes it less amenable to local customization. Latour argues that the fate of a machine or technology lies in the hands of those that come after the inventor(s). Technologies (or boundary objects) that can bind the interests of many and that can cross multiple worlds are strongest because they have durable ties and connections with many instead of a few.

4. Conclusions

Our aim has been to demonstrate that political and social considerations have played a key role in the development and diffusion of IFRS. This should not come as a surprise (Hopwood, 1994). Yet we are struck by the way in which rationales offered for the move towards IFRS as a single set of international accounting standards largely, if not completely ignore such political and social factors. Our concern is that absent some broader consideration of the political process by which accounting regulation occurs, and especially the interaction with globalization more generally, it is hard to find empirically supported rationales for the harmonization process, let alone the seemingly inexorable rise of IFRS as the "premier" or "ultimate" answer.

We have noted that three popular economic rationales for the spread of IFRS all lack empirical support. The first of these is the overstated importance of accounting information as a timely measure of firm-performance and value, leading to the frequent argument that harmonization will materially assist cross-country evaluation of firm performance. In significant capital markets at least, periodic financial reporting is likely only a very small part of the information set which investors rely on to set stock market prices. On the other hand, we have learned a great deal about the economic role of accounting information as means of facilitating the monitoring and enforcement of contractual relations (Watts and Zimmerman, 1986). We are struck by how little attention has been given to the effect of harmonization in this respect, and whether the results are positive or negative. Clearly there is scope for more research that adopts a contracting, rather than an information perspective in testing for the effects of adopting a single set of global standards.

Irrespective of the weight placed on information or contracting roles, the quality of financial reporting is obviously a key issue. However, quality has many dimensions, and the evidence so far is not convincing. Those studies that rely on the effect of voluntary adoption must overcome the problem of controlling for incentives associated with voluntary adoption, while even those studies that examine effects of mandatory adoption suggest that accounting quality effects per se are perhaps overwhelmed by institutional and regulatory features unique to specific national settings.

Finally, while the "quality" of financial reporting is a broad concept with many different measurable attributes, we also note that one property of accounting frequently mentioned in support of harmonization is comparability. Yet studies of comparability across countries typically rely on a comparison of other properties, such as value relevance, rather than directly addressing comparability per se. We therefore conclude that we know almost nothing about whether harmonization results in significantly greater comparability across countries, or whether any benefits arise from such an increase. Again, this is clearly an opportunity for further research.

Given our concerns about the lack of substantive evidence supporting what are largely economic rationales for the spread of IFRS, we turn our attention to the likely role of social and political factors.

The role of these considerations has long been recognized (Hopwood, 1994), but appears under researched. We attempt to demonstrate that political and social factors play an important role in explaining the responsibility for developing a set of international accounting standards, as well as their diffusion.

Yet, despite their apparent strength in conquering many states, recent events suggest that global governance technologies such as IFRS remain as a fragile and dynamic mix of different regulatory modes. So while governments appear increasingly willing to permit the mandatory adoption of IFRS in their jurisdictions, they are also keen to remain the final decision-maker of which set of IFRS will be adopted. Interestingly, this is a right that has been appropriated by stronger nations or even suprastate agencies such as the European. Such exercises of political will suggests that governments (either at the individual state or regional level) may be willing to outsource the *creation* of IFRS as long as they retain the final decision right as to their *adoption* within their jurisdictions.

The tussle between different regulatory groups *(private versus public)* also lends plausibility to Hopwood's essential contention that the rise of IFRS is best explained by the political interests of different stakeholder and regulatory groups in the governance of global business. The irony here is that while strong nations require others to adopt international best practice, they are also able to not adopt certain standards when situations arise. This is just one example of how recognition of the critical social and political dimensions of the accounting standard setting process can yield insights that help understand the way in which standards are developed and diffused.

That politics plays a large role in accounting standard setting at least at the national level is widely acknowledged. Skinner (2008) points to the long US history of political intervention in the process of developing an accounting standard for stock options. However, as Skinner also acknowledges, we know very little about how politics influences standard setting, and this ignorance is magnified when we move to understanding the process by which we seem to inexorably move to a single set of international standards. Clearly, this is an area with considerable future research opportunities.

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