

# THE NECESSITY FOR ACCOUNTING REGULATIONS GENERALLY ACCEPTED AT INTERNATIONAL LEVEL

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## **Abstract:**

*In a market economy, accounting convergence and normalization have as an objective organizing the operation rules of the accounting information market in order to optimize financial communication. The existence of a market implies the existence of a product. Accounting information represents the product changed on the accounting information market. This product exists only according to the rules and standards that define it. Accounting information is a “legal” specific product, because its production, presentation and dissemination must be regulated. Like other countries in transition, Romania has launched a reforming process of the financial reporting system, with the assistance of some EU member countries (France, Belgium, and United Kingdom).*

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The finality assigned to accounting is the description of periodic financial statements, called "annual accounts" or synthesis documents, which form an inseparable ensemble and must confer a true and fair image of the patrimony, financial position and results of the enterprise, in order to provide useful information for users for making economic decisions.

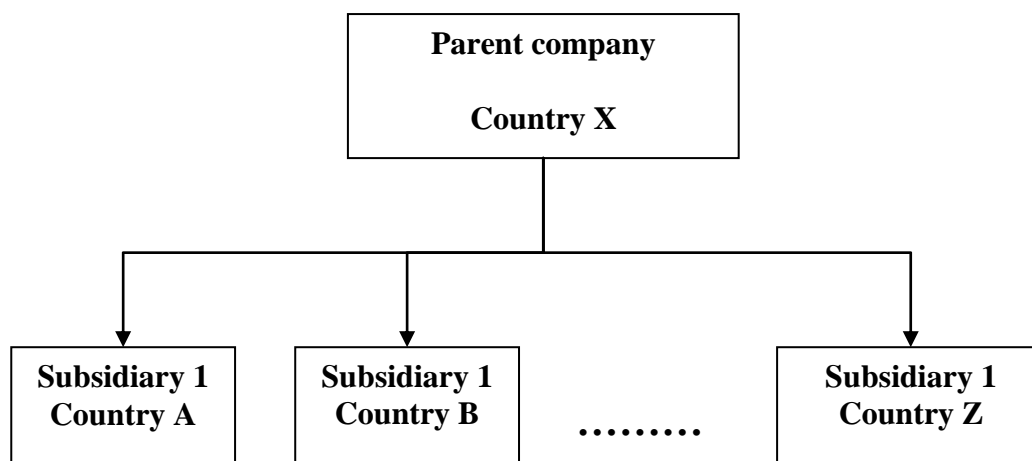
The efficient management of any patrimony unit's activity and any knowledge of the results obtained, including aspects relating to the final results, are possible in a current activity through an analysis of the data provided by financial statements.

In matters of financial reporting of information regarding the activity of various enterprises, it is particularly important and necessary to create exclusive regulations at international level. These regulations are imposed primarily by conceptual conflicts arising between those who draft financial statements, on the one hand, and those who use the information provided by them, on the other hand.

Financial statements are an accounting tool of great importance in the process management, both for the justification of decisions on the allocation, financing, use and recovery of funds, controlling the implementation of the decisions taken, as well as for the establishment of rights and obligations, responsibility and incentives from household activities and patrimony development.

In the current conditions of globalization and especially the financial ones, the differences between national accounting systems cause problems especially in multinational enterprises' activity related to two main areas: the company's internal management and securing external funding.

As its known, the operation of a multinational company implies the existence of a parent company in a given country, which controls a number of enterprises (subsidiaries), which are located in different corners of the globe.



**Fig. 1 The structure of a multinational company**

In order to ensure effective and coherent management of such a group, it is essential that all companies that compose it use the same principles in the drafting financial statements.

However, this is quite hard to achieve as long as the management of an American parent company, for example, will face difficulties in terms of assessing the performance of subsidiaries in Europe, where in German subsidiaries the assessment of its assets is made at their historical cost, and in subsidiaries in the United Kingdom their assessment is made at their fair value.

Faced with these difficulties, and not having a single set of accounting regulations at international level, in the near past, most of the multinational companies have developed a set of accounting principles to be applied by all enterprises in the group, in parallel with the mandatory provisions of the various countries in which the subsidiaries of the group operate. Thus each subsidiary was forced to report to the parent company the financial accounting information in accordance with the established principles.

This situation in which enterprises in various countries of the world were obliged to report basically two sets of financial statements (one for the local authorities and one for the parent company) has created two other difficulties in managing these enterprises.

The first of these difficulties is related to *the consistency and relevance* of this provided information. The two sets of reports can transmit different information, which can lead to confusion and uncertainty regarding the activity of that subsidiary (for example: the reports addressed to the parent company indicate a loss and the ones addressed to the local authorities indicate profit). Even if there are imposed certain principles of performance measurement by the parent company, subsidiary management will feel unjustified that they are required to carry out measurements of performance after certain principles that are not accepted at national level.

Secondly *the cost* of parallel development of the two sets of financial statements according to different accounting systems is much higher and often requires the services of an international consulting company whose rates are consequently quite large.

In other words multinational companies are in a permanent search of capital to finance their ongoing activities or the development of these activities.

When their funding needs exceed the possibilities of ensuring necessary resources by the autochthon capital markets, then they turn to the capital markets of other countries. As increasingly more multinational companies want to be quoted on the international capital markets. The reasons of such an approach are not exclusively financial, this being an advantage to other areas such as marketing (by the advertising provided to the enterprise's products on other markets than the national one) and even political (by improving relations with the Governments of those countries, the company demonstrating the active involvement in the economy of the host country). But in addition to these facts, listing a company on foreign exchanges creates a global player qualification on the world capital market (H. Stology, M. Lebas, 2002).

Listing a multinational company on various capital markets of the world is not easily achieved. Most times they will find that the financial statements drawn up by them are not accepted by those governing such foreign financial markets. In this context, in order to obtain listing on the stock exchange, enterprises are obliged to develop two sets of financial reporting, one in accordance with the their national regulations and another according to the requirements of the foreign stock exchange that they want to have access to. The inconveniences of such situations are not related only to financial considerations (relatively high cost of developing two sets of financial statements) but also by the fact that this generates a differentiated presentation of aspects such as, for example, would be the result of the exercise, which creates confusion for both investors and other users of financial statements.

The most discussed example is that of the Daimler-Crysler company (at the time Daimler Benz), a world renowned producer of cars, which operate for a long period of time as an important participant on the global capital market.

At that time (1991), company management has decided that the enterprise should become a company, known mainly in Germany, a world company, and the main objective of this strategy was the listing of its shares on the major stock exchanges of the world: London, Tokyo, Paris, Zurich, and especially on the Wall Street-New York stock exchange, the largest stock market in the world, whose market capitalization for example in 2005 was higher than that of the other following 10 world stock exchanges all together.

There are multiple reasons for the internationalization of the financial management of the enterprise and they represent a multitude of factors that are interrelated to each other. Therefore, these factors may not be presented in this chapter in an exhaustive manner, but they can be grouped, in the opinion of some authors in six categories:

a) factors arising from the globalization of production and sales activities. Are factors that arise from the need for investment or placement (placement of currency from the sale of production abroad) and from the need of means (e.g. construction of new production sites abroad through which the currency risk is annihilated);

b) restriction of the national markets for equity and foreign capital has generated an overriding necessity for large companies, active internationally to seek foreign capital markets. In this respect an important role is played not only by the question from which capital markets the corresponding volume of capital may be procured, but also, what would be the possible costs. In this respect an increasing trend of investments or the purchase of holdings (bonds), relatively cheaper than loans to banks by crediting;

c) A listing on a foreign stock exchange facilitates not only a direct purchase of capital but also facilitate multilateral access to mergers and business combination. So it was possible, after all, the first listing on a stock exchange, mentioned above, of the Daimler Benz AG company and later on (in 1998) to merge with the great American car producer Chrysler Corporation. Starting from this, the marketing strategies play an

important role, when the presence on the international capital markets increases the degree of notoriety and the distribution volume of products across borders;

d) The internationalization of financing companies has been amplified and stimulated in recent years through decentralization and openness of national capital markets. The protection of current and prospective investors everywhere from various spheres of influence generated by the application of national accounting systems is in the spotlight of international accounting standardization bodies. Enterprises wishing to gain access to certain national capital markets are obliged to prepare financial statements in accordance with the practices adopted in that particular country;

e) Establishing of a unit within the European economic area. Of great importance for EU Member States was the European Commission's recommendation according to which all listed entities should draw up beginning with fiscal 2005 consolidated financial statements in accordance with IFRS. At European level, this recommendation is basically the most significant change in the accounting system since the appearance of the European directives on accounting and until present;

f) The development of information and communication technologies, representing a powerful catalyst to all the factors mentioned above.

The diversity of accounting systems in the world is therefore an easily established fact. We can reasonably think that economic development marked by the internationalization of markets and enterprises' activities, especially the growth of direct international investments, will determine that more and more Nations try to approximate their accounting systems. This proximity is strongly requested by international investors, who want to be able to compare, in a guaranteed manner and after equivalent criteria, the capital placement opportunities. Many comparative studies have shown that, according to the methods used in different countries, the results of the same enterprise were slightly different. For reasons of respecting equality in competition, many voices arose that demanded fair treatment of enterprises, subjecting them to common regulations for the publication of financial information.

Moreover, internal and external investors need information about enterprise, about equity and foreign capital available or that will be made available. Based on the detained information, they want to evaluate how profitable was the enterprise in the past and to conclude, decide on the expected profits in the future. Investors can therefore decide whether they will maintain, increase or liquidate the investment in the future. The informing tool, which in almost all States of the world is made available to investors by law both in general (for example in Germany, France, etc.) or at least in the case of an enterprise listed on a stock exchange (e.g. in the USA), is represented by the financial statements, both the individual and consolidated.

The issue arises from the fact that the published financial statements are based on regulations valid at national level. These financial statements elaborated on the basis of national accounting reference guide are not sufficient to meet the requirements of the supervisory authorities of foreign exchange.

Despite numerous attempts of convergence between the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB), the so-called "Norwalk Agreement", the United States Securities and Exchange Commission (SEC) accepts only financial statements elaborated in accordance with the American accounting standards, which are in accordance with the United States-Generally Accepted Accounting Principles (US GAAP). Formally, SEC does not preclude the financial statements elaborated according to other accounting standards. But the Commission claims that all major differences compared to the accounting principles and methods accepted by it for each position in the balance sheet and in the profit and loss account to be exposed and quantified, therefore restated. In fact,

presenting and quantifying those differences and influences means the elaboration of new financial statements, in particular in accordance with US-GAAP.

This will (probably) change in the foreseeable future, since the EU-Commission and SEC have come to the understanding that the companies that elaborate financial statements according to IFRS should no longer be forced to make adjustments for compliance with US-GAAP, in order to allow them access to the American capital markets.

There is also the danger that the financial statements elaborated according to the national regulations would be misinterpreted by an investor or that they lead to prejudices to a potential investor. In special cases this also applies for the continental European States.

They are subject to the national rules and regulations, which in most cases are not recognized internationally. Therefore, both from those who want capital and those that offer capital, it is desirable that the elaboration of financial statements is made according to internationally agreed regulations.

The need for harmonization and uniformity in accounting entails approximation. In this way the objectives, concepts, methods, regulations and procedures on the production and use of the accounting information are formalized and materialized.

The normalization effort as well as its product reflects in:

- a) the definition of the concepts, principles and accounting standards based on a precise terminology and identical for all producers and users of accounting information;
- b) their practical implementation in order to ensure comparability in time and space, relevance and reliability of accounting information.

Normalization has as a main objective the financial statements (own Anglo-Saxon countries and relates to: the components of the financial statements, the elements presented in them, recognizing and evaluating them, etc) or the general accounting plan (own by continental accounting and refers to the system of accounts, mailing rules, rules on the presentation of financial statements, accounting organization etc.). Normalization may take several forms: normalization imposed by normative acts (legal or regulated) and professional normalization (standards issued by the relevant professional organizations). It goes without saying that these two categories are interrelated and influence each other.

Accounting legal framework is based on a set of regulations and provisions included in: accounting law, accounting or conceptual framework, network accounting regulations or standards; accounting regulatory system (accounting law), and chart of accounts and scheme of using economic operations, professional guides, to the normalization accounting institution.

These regulations may be ranked according to their importance as follows: rules contained in treaties or international agreements (having superiority and priority over national law provided that they are applied also by the other party), legislative texts (laws and decrees stating the important matters limited imperative by the Constitution), jurisprudence elements (decisions of the courts, whose task it is to ensure the examination of litigation appeals on which they are notified, the laws were implemented; this is not mandatory) and doctrine (consisting of interpretations or notices regarding the items on which the legislative and regulatory texts have not been specified: ministerial responses, recommendations from various bodies etc.).

## **Conclusions**

Eliminating borders in businesses by increasing globalization entailed a movement towards a borderless accounting in order to eliminate the anomalies of different accounting systems. Within synchronic and diachronic dichotomy, synchronicity defines the axis of simultaneity and diachronic the successive axis. While

synchronic leads to globalization, permitting permanence in classification and evaluation, framework in which we consider suitable terms such as compliance, convergence, and the diachronic stops the permanence in favor of changes. By convergence we understand a movement towards the same point between the accounting systems, and by compliance we understand accordance with something predetermined.

Concluding, we can affirm that using a single accounting referential can be beneficial for all stakeholders interested in financial reporting, because only in this way it accounting becomes credible, entities have easier and cheaper access to capital markets and financial statements auditing generates lower costs.

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