

**IT'S GREEK TO ME: THE CASE FOR CREATING AN  
INTERNATIONAL AGENCY TO ENFORCE  
INTERNATIONAL ACCOUNTING STANDARDS TO  
PROMOTE HARMONIZATION AND INTERNATIONAL  
BUSINESS TRANSACTIONS**

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**INTRODUCTION**

The harmonization of accounting standards provides transparent and comparable financial statements for the international business community, helping investors and other financial statement users make decisions. To help ensure uniform compliance across the globe, there needs to be an international accounting standards regulatory body that would monitor the financial statements created by companies doing business internationally. Without an enforcement mechanism, countries would have the ability to apply the accounting standards in any manner in which they see fit, and thus defeat the purpose of the international accounting standards.

While the global accounting market is shifting towards harmonization of accounting standards, one problem still remains on the horizon: lack of enforcement.<sup>1</sup> The purpose of harmonization is to provide more transparent and comparable financial statements to help investors make investment decisions.<sup>2</sup> In an effort to make financial statements more transparent across the globe, many countries are adopting the accounting standards set forth by the International Accounting Standards Board (IASB), an independent standard setting body located in the United

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<sup>1</sup> Sabine D. Selbach, *The Harmonization of Corporate Taxation & Accounting Standards in the European Community and Their Interrelationship*, 18 *CONN. J. INT'L L.* 523, 558 (Spring, 2003); Maureen Peyton King, *The SEC's Changing Stance on IAS*, 27 *BROOKLYN J. INT'L L.* 315, 342 (2001).

<sup>2</sup> Scott B. Novak, *A Step Toward Globalization: The Move for International Accounting Standards*, 9 *IND. INT'L & COMP. L. REV.* 203, 222 (1998); Bert J. Zarb, *The Quest for Transparency in Financial Reporting: Should International Financial Reporting Standards Replace U.S. GAAP?*, *THE CPA JOURNAL*, Sep. 1, 2006, 30.

Kingdom.<sup>3</sup> These standards, known as “international financial reporting standards” (IFRS), as well as the international accounting standards (IAS) set forth by the IASB’s predecessor, the International Accounting Standards Committee (IASC), are designed to create more uniform financial statements as companies continue to expand their business from nation to nation.<sup>4</sup> With a common set of international accounting standards, when companies create their financial statements, they will be using the same financial language as well as applying the same set of rules.<sup>5</sup>

The IFRS and the IAS affect the way multinational companies (MNCs) report their earnings to investors and for tax purposes.<sup>6</sup> MNCs report earnings to the government of the countries in which they do business.<sup>7</sup> MNCs have more difficulty obtaining “finance” in countries that do not adopt the use of IFRS.<sup>8</sup> Thus, companies will be more hesitant to do business in those countries.<sup>9</sup> In theory, the harmonization of accounting will increase the efficiency of global business; however, the lack of an enforcement agency will undercut the harmonization process because it will undermine the legitimacy of the operation.<sup>10</sup>

This Comment argues that the international community must create an enforcement agency to oversee global accounting practices in order for global accounting standards to be harmonized and therefore more transparent. One way to achieve harmonization is for countries to yield lawmaking power to an international regulator or agency.<sup>11</sup> Without an international enforcement agency, individual countries may enforce the accounting standards in different fashions, defeating the purpose of implementing the harmonized standards.<sup>12</sup>

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<sup>3</sup> Stephen A. Zeff, *U.S. GAAP Confronts the IASB: Roles of the SEC and the European Commission*, 28 N.C.J. INT’L L. & COM. REG. 879, 885-887 (Summer, 2003); Michael P. Cangemi, *The Challenge of Global Accounting Convergence*, FINANCIAL EXECUTIVE, July 1, 2007, 6

<sup>4</sup> *Id.*

<sup>5</sup> See King, *supra* note 1, at 326.

<sup>6</sup> Michele C. Osborn, *Accounting Standards: Nationally or Internationally Set?*, THE OHIO CPA JOURNAL, October 1, 2001.

<sup>7</sup> See *id.*

<sup>8</sup> Geoffrey Pickard, *Simplifying Global Accounting: IASB Chair Discusses the Future of IFRS, U.S. GAAP and the Global Accounting Profession*, JOURNAL OF ACCOUNTANCY, July 1, 2007, 36.

<sup>9</sup> See *id.*

<sup>10</sup> Thomas M. Franck, *Legitimacy in the International System*, 82 A.J.I.L. 705, 706 (Oct. 1988).

<sup>11</sup> Tzung-bor Wei, *The Equivalence Approach to Securities Regulation*, 27 NW. J. INT’L. & BUS. 255, 255 (Winter, 2007).

<sup>12</sup> Bernhard Grossfeld, *Global Accounting: Where Internet Meets Geography*, 48 AM. J. COMP. L. 261, 277 (Spring, 2000); Clyde Stoltenberg et al. *A Comparative Analysis of Post-Sarbanes-*

Part I of this Comment will discuss the purpose of the harmonization of international accounting standards. Part II explores the growing trend towards the harmonization of accounting standards by examining the measures the different nations are taking to overhaul their past accounting systems to implement the IASB's standards. In Part III, this comment will argue that for the harmonization of accounting standards to be effective, there needs to be an international governing body to oversee the compliance with the standards. Part III will include a comparison between this proposed international governing body and the U.S. Securities and Exchange Commission (SEC) as well as international regulatory actions such as the Kimberly Process and the International Labor Organization.

## I. THE PURPOSE OF HARMONIZATION

The globalization of business has caused the need for one common accounting language that can be understood worldwide.<sup>13</sup> To solve that problem, there has been a push within the past two decades to create a set of international accounting standards that are accepted across the globe.<sup>14</sup> By adopting one common set of international accounting standards, countries aid the efficiency of international business in two ways: first, financial statements will be easier to compare and second, companies will cut costs by only having to create one set of financial statements.<sup>15</sup>

### A. EASIER COMPARABILITY

Without having an accepted set of international accounting standards, financial statements are not easily comparable between companies based in different countries.<sup>16</sup> The differences in these financial statements make it difficult for investors to make informed investment deci-

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*Oxley Corporate Governance Developments in the U.S. and European Union: The Impact of Tensions Created by Extraterritorial Application of Section 404*, 53 AM. J. COMP. L. 457, 486-487 (Spring, 2005).

<sup>13</sup> Charles Canfield, *FASB v. IASC: Are the Structure and Standard Setting Process at the IASC Adequate for the Securities and Exchange Commission to Accept International Accounting Standards for Cross-Border Offerings?*, 20 NW. J. INT'L L. & BUS. 125, 128 (Fall, 1999).

<sup>14</sup> *Id.*

<sup>15</sup> Osborn, *supra* note 6.

<sup>16</sup> *Id.*

sions based on a company's performance.<sup>17</sup> Typically, national investors understand the local variations in the accounting standards; however, with global business, investors are more nationally diverse and they often lack the understanding of these local variations.<sup>18</sup> In 2001, the European Commission stated that, "the most effective basis for ensuring this objective of comparability is a requirement for listed companies to publish financial statements that conform to a single set of standards."<sup>19</sup> The move towards harmonization stems from the difficulties that arise from using different sets of accounting standards.<sup>20</sup>

Nokia, a Finnish company, and its financial statements from 1995 are an example of the disparities that arise as a result of lack of comparability.<sup>21</sup> Nokia reported net profits of 1971 million Markka under Finnish accounting standards, 2,232 million Markka under IAS, and 2,162 million Markka under U.S. Generally Accepted Accounting Principles (GAAP).<sup>22</sup> This discrepancy left investors wondering which number most accurately reflected Nokia's financial position.<sup>23</sup> Another example involves the German company Daimler-Benz AG. In 1993, the company posted its 1992 financial results on the New York Stock Exchange.<sup>24</sup> Under U.S. GAAP, the company had a loss of Deutsche Mark 949 million; however, under German accounting laws the company reported a profit of Deutsche Mark 168 million.<sup>25</sup> Once again, an investor would have difficulty determining Daimler-Benz AG's accurate financial position. While investors will be helped through the clarity of financial statements produced under one set of accounting standards, businesses will also be helped in their bottom line.<sup>26</sup>

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<sup>17</sup> David S. Ruder, Charles T. Canfield and Hudson T. Hollister, *Creation of World Wide Accounting Standards: Convergence and Independence*, 25 NW. J. INT'L L. & BUS. 513, 568 (Spring, 2005).

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

<sup>20</sup> See Osborn, *supra* note 6.

<sup>21</sup> James D. Cox, *Regulatory Duopoly in U.S. Securities Markets*, 99 COLUM. L. REV. 1200, 1212 (June, 1999).

<sup>22</sup> *Id.*

<sup>23</sup> *Id.*

<sup>24</sup> Selbach, *supra* note 1 at 559.

<sup>25</sup> *Id.*

<sup>26</sup> Ruder, *supra* note 17; Osborn, *supra* note 6.

## B. COSTS CUTTING

The other goal of the harmonization of international accounting standards is to reduce companies' costs.<sup>27</sup> Without harmonization, a company would have to create financial statements under each country's GAAP in which it does business.<sup>28</sup> The process requires additional costs in terms of having additional personnel to understand multiple financial accounting standards for both the companies preparing the financial statements as well as those interpreting them.<sup>29</sup> Having one set of globally accepted accounting standards will reduce the direct costs of creating multiple financial statements.<sup>30</sup> Additionally, it will reduce the indirect costs of the employees' time of creating the statements, time which could be spent doing other work.<sup>31</sup> For example, foreign companies that want to be listed on the New York Stock Exchange and other U.S. stock exchanges are required to reconcile their financial statements in accordance to U.S. GAAP.<sup>32</sup> A 2005 report indicated that the largest EU companies listed in the U.S. spend between \$1 million and \$10 million to reconcile their financial statements from the international accounting standards to U.S. GAAP.<sup>33</sup> Additionally, companies experience increased costs of capital because of the investors' confusion caused by reconciling financial statements from one country's GAAP to another's.<sup>34</sup> One set of international financial standards accepted globally will eliminate these extra costs and will increase the efficiency of the international business world.<sup>35</sup>

## II. THE ROAD TO HARMONIZATION

This section will examine the different international accounting standard setting organizations and their role in the harmonization

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<sup>27</sup> Robert H. Herz and Kimberley R. Petrone, *International Convergence of Accounting Standards—Perspectives from the FASB on Challenges and Opportunities*, 25 NW. J. INT'L L. & BUS. 631, 632 (Spring, 2005).

<sup>28</sup> *Id.*

<sup>29</sup> *See id.*

<sup>30</sup> Stuart H. Deming, *International Financial Reporting Standards: Their Importance to U.S. Business and Legal Practice*, 84 MI BAR JNL. 14, 16 (December 2005).

<sup>31</sup> *Id.*

<sup>32</sup> Zarb, *supra* note 2.

<sup>33</sup> Wei, *supra* note 11 at 283.

<sup>34</sup> Stavros Gadinis, *The Politics of Competition in International Financial Regulation*, 49 HARV. INT'L L.J. 447, 477-78 (Summer 2008).

<sup>35</sup> Herz, *supra* note 27.

process. The section will also describe different nations that have adopted international accounting standards. Finally, this section will argue that harmonization is only part of the global uniformity of international financial statements because the current system lacks a uniform enforcement mechanism.

### A. THE HISTORY OF HARMONIZATION

In 1973, the International Accounting Standards Committee (IASC) was established as an international accounting standards setting body.<sup>36</sup> The nine countries that formed the IASC were Australia, Canada, France, Germany, Japan, Mexico, Holland, the United Kingdom (with Ireland), and the United States.<sup>37</sup> Sixteen voting delegations and five non-voting delegations comprised the board through which the IASC conducted its business.<sup>38</sup> The board delegates were volunteers and worked only part-time.<sup>39</sup>

The purpose of the IASC was “to achieve harmony among accounting principles used by enterprises and other organizations for financial reporting around the world.”<sup>40</sup> The IASC produced accounting standards known as international accounting standards (IAS).<sup>41</sup> Initially, the IASC developed IAS comprised of practices used in a variety of countries, but these standards allowed for multiple treatments for some transactions.<sup>42</sup> Instead of making financial statements more uniform, these initial IAS caused more murkiness than they helped.<sup>43</sup>

In 1993, the International Organization of Securities Commissions (IOSCO) developed forty standards, which it concluded were necessary to assist in promoting the transparency of international financial statements.<sup>44</sup> The IOSCO is an international organization consisting of

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<sup>36</sup> Mark J. Hanson, *Becoming One: The SEC Should Join the World in Adopting the International Financial Reporting Standards*, 28 *LOY. L.A. INT'L & COMP. LAW REV.* 521, 524 (Summer, 2006).

<sup>37</sup> CLARE ROBERTS ET AL., *INTERNATIONAL FINANCIAL ACCOUNTING: A COMPARATIVE APPROACH* 133 (Prentice Hall 2002).

<sup>38</sup> Report on Promoting Global Preeminence of American Securities Markets, SEC (Oct. 1997), <http://www.sec.gov/news/studies/acctgsp.htm> (last visited Oct. 20, 2007).

<sup>39</sup> *Id.*

<sup>40</sup> Canfield, *supra* note 13.

<sup>41</sup> *Id.* at 126.

<sup>42</sup> *Id.* at 127.

<sup>43</sup> *See id.*

<sup>44</sup> *Id.* at 128.

securities agencies from various nations, and the organization is “the world’s most important international cooperative forum for securities regulatory agencies.”<sup>45</sup> The IOSCO stated “the necessary components of a reasonably complete set of accounting standards (core standards) that would comprise a comprehensive body of [accounting] principles for enterprises undertaking cross-border offerings and listings.”<sup>46</sup> The standards’ goals were to produce quality reliable financial information, to adapt to divergence in application, and to be enforceable.<sup>47</sup>

In 1995, IOSCO declared that fourteen of the existing IASs did not require additional work, leaving twenty-six that needed to be designed to finish its plan of forty; IOSCO gave the IASC until March 1998 to come up with these standards.<sup>48</sup> However, the IASC did not meet the March 1998 deadline, failing to complete four standards.<sup>49</sup> During this time period, the IASC came under strong criticism for being a part-time accounting standards setting Board and for having insufficient technical staff to execute the convergence of international accounting standards.<sup>50</sup> In essence, the IASC did not have the man power or ability to bring about the harmonization of the international accounting standards that the IOSCO wanted.<sup>51</sup>

The board yielded to the criticisms and it restructured itself into the International Accounting Standards Board (IASB).<sup>52</sup> The IASB is comprised of fourteen board members: twelve full-time and two part-time.<sup>53</sup> The IASB has the same purpose as its predecessor, namely to de-

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<sup>45</sup> IOSCO.org, IOSCO Historical Background, <http://www.iosco.org/about/index.cfm?section=history> (last visited Oct. 21, 2007). The member nations have resolved the following: “to cooperate together to promote high standards of regulation in order to maintain just, efficient, and sound markets; to exchange information on their respective experiences in order to promote the development of domestic markets; to unite their efforts to establish standards and an effective surveillance of international securities transactions; to provide mutual assistance to promote the integrity of the markets by a rigorous application of the standards and by effective enforcement against offenses.” IOSCO.org, General Information on IOSCO, <http://www.iosco.org/about/> (last visited Sep. 30, 2007).

<sup>46</sup> Janice Grant Brunner, *All Together Now? The Quest for International Accounting Standards*, 20 U. PA. J. INT’L ECON. L. 911, 913 (Winter, 1999).

<sup>47</sup> Paul Pacter, *International Accounting Standards: The World’s Standards by 2002*, THE CPA JOURNAL, 18 (July 1998).

<sup>48</sup> *Id.* at 128-129.

<sup>49</sup> *Id.* at 129.

<sup>50</sup> Zeff, *supra* note 3, at 885.

<sup>51</sup> *Id.*

<sup>52</sup> *Id.* at 886.

<sup>53</sup> *Id.*; About IASB, IASB, <http://www.iasb.org/About+Us/About+IASB/About+IASB.htm> (last visited Oct. 20, 2007).

sign one set of international accounting standards that create transparent and comparable financial statements.<sup>54</sup> The IASB adopted the IAS as its accounting standards and the Board created its own standards, known as international financial reporting standards (IFRS).<sup>55</sup> IFRS, like their predecessors, IAS, are principle based standards, which means that they “specify how the concepts in the framework apply to the topic of the particular standard.”<sup>56</sup> The principles set forth by the IFRS are stated in such a manner that indicates that they are requirements and not merely guidelines.<sup>57</sup> Once the IASB was created, it began moving towards achieving its goal of providing one set of uniform accounting standards accepted worldwide.<sup>58</sup>

### B. THE IASB’S MOVEMENT TOWARDS HARMONIZATION

There are many advantages for countries to adopt the IFRS as their national accounting standards.<sup>59</sup> One of these advantages is the reduced costs of capital because one set of financial statements can be used from country to country; there would not be the need to spend money to conform the statements to the local rules.<sup>60</sup> The other advantage is the clarity the single financial statements provide for investors.<sup>61</sup> Currently there are nearly 100 nations that require, permit, or have plans to converge with IFRS, and the chair of the IASB, Sir David Tweedie, believes that the number will rise to 150 countries.<sup>62</sup>

Tweedie is worried that as nations begin adopting the IFRS as the national accounting standard, they will do so using a national flare.<sup>63</sup> For instance, Australia adopted IFRS, but the Australians referred to

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<sup>54</sup> About IASB, *supra* note 53; Cangemi, *supra* note 3; Mary E. Barth, *Globalization of Financial Reporting*, FOUNDATIONS AND TRENDS IN ACCOUNTING, Nov. 1, 2006, 129.

<sup>55</sup> Hanson, *supra* note 36, at 521.

<sup>56</sup> Lawrence M. Gill, *IFRS: Coming to America: What CPAs Need to Know About the New Global GAAP*, JOURNAL OF ACCOUNTANCY, June 1, 2007, 70; Barth, *supra* note 54.

<sup>57</sup> Barth, *supra* note 54. The IASB creates their principles to state that an entity “shall do whatever the principle says.” *Id.*

<sup>58</sup> Cangemi, *supra* note 3.

<sup>59</sup> Deming, *supra* note 31.

<sup>60</sup> *Id.*

<sup>61</sup> *Id.*

<sup>62</sup> IFRS Around the World, IASB, <http://www.iasb.org/About+Us/About+IASB/IFRS+Around+the+World.htm> (last visited Oct. 20, 2007); Pickard, *supra* note 7.

<sup>63</sup> *Id.*



them as Australian International Financial Reporting Standards.<sup>64</sup> These standards were in fact IFRS.<sup>65</sup> However, outsiders did not know that fact because the word Australia was in the title, leaving outsiders to think they were merely local accounting standards.<sup>66</sup> Australia solved the problem by removing the word Australia from in front of the financial standards.<sup>67</sup>

Additionally, Tweedie was worried nations would state that their accounting standards were based on IFRS.<sup>68</sup> He was anxious that the market would contain these diluted accounting standards which would confuse users of these tainted financial statements.<sup>69</sup> Despite these minimal concerns, Tweedie is confident that the international harmonization process will continue to gain momentum.<sup>70</sup> The following examples reflect Tweedie's concerns with the harmonization process.

The European Union currently requires its members to use the international accounting standards.<sup>71</sup> However, it faced two challenges when deciding whether to use the international accounting standards (1) using IFRSs or creating its own standards based on IFRS (national flare issue) and (2) strict adherence to the rules.<sup>72</sup> In 2002, the European Union established a plan to adopt the IFRSs as its accounting standards for all of its listed companies by 2005.<sup>73</sup> The adoption of the IASs and IFRSs applied not only to members of the European Union, but also to members of the European Economic Area (e.g., Norway).<sup>74</sup>

The European Commission rejected having a separate European set of accounting standards.<sup>75</sup> The Commission felt it would be detrimental for the European Union to operate a "fortress Europe" and isolate itself from the global financial markets thereby damaging the EU's com-

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<sup>64</sup> *Id.*

<sup>65</sup> *Id.*

<sup>66</sup> *Id.*

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> *See id.*

<sup>70</sup> *Id.*

<sup>71</sup> *See Selbach, supra note 1, at 553.*

<sup>72</sup> Kennard S. Brackney & Philip R. Witmer, The European Union's Role in International Standards Setting: Will Bumps in the Road to Convergence Affect the SEC's Plans?, *THE CPA JOURNAL*, Nov. 1, 2005, 18; Selbach, *supra note 1, at 553*; Floyd Norris, *A Plan to Let S.E.C. Accept Foreign Rules Is Opposed*, *N.Y. TIMES*, September 25, 2007, at C4.

<sup>73</sup> Brackney, *supra note 72.*

<sup>74</sup> Geoffrey Whittington, *The Adoption of International Accounting Standards in the European Union*, 14 *EUR. ACCT. REV.* 127, 127 (May 2005).

<sup>75</sup> Selbach, *supra note 1, at 553.*

petitiveness in the world economy.<sup>76</sup> Instead the Commission said the EU should adopt the international accounting standards.<sup>77</sup> Nevertheless, the Commission did allow the EU to deviate from the IFRS.<sup>78</sup> The deviation does not require European companies to comply with the IFRS for accounting for derivatives.<sup>79</sup> Such a minor change to the accounting standards undermines the entire harmonization process because it creates a scenario in which the financial statements will not be uniform from country to country.<sup>80</sup>

China is another nation that recently moved towards integrating the use of international accounting standards.<sup>81</sup> In February 2006, the ministry of finance revealed the Chinese Accounting Standards for Business Enterprises, basic accounting standards and thirty-eight specific accounting standards.<sup>82</sup> Winnie Cheung, the Chief Executive and Register of the Hong Kong Institute of Certified Public Accountants (HKICPA) stated that by converging with the international standards, China will be able “to speak the same financial language as companies in the rest of the world” and the transparent financial statements will help attract overseas funding.<sup>83</sup> China, following Australia’s footsteps, adopted some of the IFRS but kept a national name for its accounting standards.<sup>84</sup> As of March 2007, China’s accounting standards were still in flux, and there was a “weakening of financial disclosure.”<sup>85</sup> However, the Chinese standards have become closer in nature to the IFRS in the past year.<sup>86</sup>

Even though Tweedie expressed optimism that that the harmonization process would spread globally, the harmonization momentum has not been enough to change the way accounting is performed in the United States.<sup>87</sup> The United States has not adopted the IFRS as a part of its

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<sup>76</sup> Selbach, *supra* note 1, at 553-554.

<sup>77</sup> *Id.*

<sup>78</sup> Norris, *supra* note 72.

<sup>79</sup> *Id.*

<sup>80</sup> *See id.*

<sup>81</sup> Allan Nam, *A Steady Move Towards Meeting Global Standards*, SOUTH CHINA MORNING POST, Apr. 26, 2007, at 4.

<sup>82</sup> *Id.*

<sup>83</sup> *Id.*

<sup>84</sup> Nam, *supra* note 81; Pickard, *supra* note 8.

<sup>85</sup> *Paulson's Realism on China*, SECURITIES INDUSTRY NEWS, March 19, 2007.

<sup>86</sup> Enoch Yiu, *Deloitte Chief Seizes on Mainland Opportunities*, SOUTH CHINA MORNING POST, June 9, 2008, 12.

<sup>87</sup> *See Jennifer Hughes, Fast Adoption Raises Hopes of Happy Families*, FINANCIAL TIMES, Sep. 10, 2007, 2.

GAAP.<sup>88</sup> Currently, the United States relies upon the Statements of Financial Accounting Standards (SFAS) and other pronouncements created by the Financial Accounting Standards Board (FASB).<sup>89</sup> The accounting standards produced by the FASB are rules based standards, and the difference in the underlying principles between U.S. GAAP and the IFRS result in different asset valuation, which could lead to differences in reported net income and retained earnings.<sup>90</sup>

Despite these differences, the two organizations, the FASB and the IASB, have been working on convergence of their standards.<sup>91</sup> In 2002, the FASB and the IASB signed the Norwalk Agreement, “in which both organizations agreed to work together to promote convergence.”<sup>92</sup> During the meeting for the Norwalk Agreement, the FASB and IASB vowed to do the following “(a) make their existing financial reporting standards fully compatible as soon as is practicable; and, (b) to coordinate their future work programs to ensure that once achieved, compatibility is maintained.”<sup>93</sup>

The Norwalk Agreement has already shown promise through IFRS 8, the standard for reporting business segments, which was based in large part on the U.S. standard of the same subject.<sup>94</sup> In spite of the apparent success of the agreement and the steps taken by both organizations towards harmonization, IFRS 8 came under heavy scrutiny from the European community.<sup>95</sup> The European community feared that the IASB would be unduly influenced by the FASB, and that eventually the international accounting standards would be tailored towards the U.S. GAAP

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<sup>88</sup> *Id.*

<sup>89</sup> FASB.org, Facts About FASB, <http://www.fasb.org/facts/index.shtml> (last visited Oct. 21, 2007).

<sup>90</sup> Gill, *supra* note 55.

<sup>91</sup> Hanson, *supra* note 36, at 530.

<sup>92</sup> *Id.*

<sup>93</sup> FASB.org, Memorandum of Understanding: “The Norwalk Agreement”, <http://www.fasb.org/news/memorandum.pdf> (last visited Oct. 21, 2007). The organizations agreed to achieve the compatibility the following are of high priority (a) undertake a short-term project aimed at removing a variety of individual differences between U.S. GAAP and International Financial Reporting Standards (IFRSs, which include International Accounting Standards, IASs); (b) remove other differences between IFRSs and U.S. GAAP that will remain at January 1, 2005, through coordination of their future work programs; that is, through the mutual undertaking of discrete, substantial projects which both Boards would address concurrently; (c) continue progress on the joint projects that they are currently undertaking; and, (d) encourage their respective interpretative bodies to coordinate their activities. *Id.*

<sup>94</sup> Jennifer Hughes, *Fast Adoption Raises Hopes of Happy Families*, FINANCIAL TIMES, Sep. 10, 2007, 2.

<sup>95</sup> *Id.*

as opposed to the U.S. GAAP becoming tailored towards the IFRS.<sup>96</sup> Despite this trepidation, the talks between the international accounting community and the U.S. have continued.<sup>97</sup>

Recently, there was a proposal by the SEC to allow foreign companies to use international accounting standards when filing with U.S. regulators.<sup>98</sup> Currently, those companies whose securities are registered with the SEC have to either submit their filings in according to the U.S. GAAP or they have to reconcile them to GAPP.<sup>99</sup> However, the proposal has run into opposition on both the domestic and international fronts.<sup>100</sup> The European Commission suggested that the U.S. require European companies to follow its accounting modifications instead of strictly adopting the international accounting standards.<sup>101</sup> The rationale behind the Commission's suggestion is that it would be confusing to investors looking at European companies' financial statements prepared using the European version if they were redone using IFRS.<sup>102</sup>

The domestic criticisms arose out of the Investors Technical Advisory Committee, a group that advises the FASB, about the differences between the international accounting system and the U.S. accounting system.<sup>103</sup> Jack Ciesielski, a member of the Committee, stated that there were too many material differences between the international and the U.S. accounting systems. He said that if there was no reconciliation, then there would not be a proper way to estimate the differences between the two accounting systems.<sup>104</sup> On behalf of the Committee, Ciesielski expressed concern about whether there was "consistent auditing and enforcement" of the international accounting standards.<sup>105</sup>

On August 27, 2008, with the prospect of allowing foreign companies to use international accounting standards when filing within the U.S., the SEC proposed a road map that would move the U.S. away from its own set of financial standards and towards adopting the international

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<sup>96</sup> *Id.*

<sup>97</sup> Norris, *supra* note 72.

<sup>98</sup> *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> *Id.*

<sup>101</sup> *Id.*

<sup>102</sup> *Id.*

<sup>103</sup> *Id.*

<sup>104</sup> *Id.*

<sup>105</sup> *Id.*

accounting standards.<sup>106</sup> The SEC formally issued its proposal on November 14, 2008 for a 90-day comment period.<sup>107</sup> As an initial step under the plan, the SEC would allow 110 of the largest American firms to use international accounting standards for financial statements issued after December 15, 2009.<sup>108</sup> Eventually, the SEC said it would consider requiring all U.S. companies to use IFRS by no later than 2016.<sup>109</sup> The SEC will make its determination on the mandatory use of IFRS for U.S. filings by 2011.<sup>110</sup> By allowing some companies to avoid using U.S. standards now, the SEC will make it difficult for future chairmen to require foreign companies to strictly use U.S. standards.<sup>111</sup> Thus, the SEC made a big leap forward in the harmonization process.<sup>112</sup>

Once harmonization is accomplished, the international community needs to address the issue of enforcement. Without a means of uniform enforcement, accounting standards get applied differently in different countries, and the goal of financial statement clarity is undermined.<sup>113</sup>

### C. PROBLEMS WITH ENFORCEMENT

While there is a movement towards the harmonization of international accounting standards, there is not in place an international enforcement mechanism to ensure compliance with the standards.<sup>114</sup> Currently, the enforcement of the standards is left to the responsibility of the individual nations and their regulatory bodies.<sup>115</sup> The FASB gathers its power and authority as a standard setter from the SEC policy to only accept FASB-created standards (which are created in accordance to U.S.

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<sup>106</sup> Floyd Norris, *U.S. Moving to Adopt International Accounting Standards*, THE INTERNATIONAL HERALD TRIBUNE, Aug. 29, 2008, at 11.

<sup>107</sup> JournalofAccountancy.com, U.S. CPAs Show Growing Acceptance of Change from U.S. to International Accounting Standards, <http://www.journalofaccountancy.com/Web/CPAsShowAcceptanceofIFRS> (last visited Jan. 5, 2009).

<sup>108</sup> Norris, *supra* note 106, at 11.

<sup>109</sup> *Id.*

<sup>110</sup> *Id.*

<sup>111</sup> *Id.*

<sup>112</sup> *See id.*

<sup>113</sup> Karel Lannoo, *The Emerging Framework for Disclosure in the EU*, 3 J. CORP. L. STUD. 329, 355 (2003).

<sup>114</sup> King, *supra* note 1, at 242.

<sup>115</sup> Stephen J Choi, *What We Know and Do Not Know About the Impact of Civil Justice on the American Economy and Policy: Law, Finance, and Path Dependence: Developing Strong Securities Markets*, 80 TEX. L. REV. 1657, 1702 (June, 2002).

GAAP).<sup>116</sup> The SEC provides the FASB with the enforcement power that the IASB currently lacks.<sup>117</sup>

On the international stage, skeptics doubt how uniformly the international accounting standards will be enforced.<sup>118</sup> This skepticism did not begin just after the creation of the IASB.<sup>119</sup> Rather, the IOSCO expressed concerns about who would enforce the IASB's core standards.<sup>120</sup> Even though IOSCO endorses the use of IFRS and IAS for its member bodies, it can only recommend their use; it cannot require their use.<sup>121</sup> Likewise, even though a country adopts the international accounting standards as its GAAP, this adoption does not ensure that those countries will comply with them or enforce them.<sup>122</sup> The Committee of European Securities Regulators (CESR) understood the need for providing a means to ensure uniform enforcement within the EU.<sup>123</sup> The CESR noted that without a consistent approach, "the rules will wrongly be customized in different EU member states."<sup>124</sup> The following are examples of specific instances where adoption of the international accounting standards did not necessarily lead to strict compliance.

For example, in 2003, Portugal followed the IAS 34 format for its biannual reporting, while its quarterly reporting required far less information.<sup>125</sup> Even though Portugal endorses the use of international accounting standards, it does not enforce them during the quarterly reporting periods.<sup>126</sup> This allows financial statements to be released that are not as easily compared or as transparent as those released by other EU nations that have adopted the use of international accounting standards.<sup>127</sup>

A second example illustrating the problem with enforcement involves the EU's adoption of IAS 39.<sup>128</sup> IAS 39 deals with derivative ac-

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<sup>116</sup> Novak, *supra* note 2 at 223.

<sup>117</sup> *See id.*

<sup>118</sup> Luca Enriques, EC Company Law Directives and Regulations: How Trivial Are They?, 27 U. PA. J. INT'L ECON. L. 1, 45 (Spring, 2006); Bernard S. Black, The Legal and Institutional Preconditions for Strong Securities Markets, 48 UCLA L. REV. 781, 824 (April, 2001).

<sup>119</sup> Osborn, *supra* note 6.

<sup>120</sup> *Id.*

<sup>121</sup> Whittington, *supra* note 74 at 132.

<sup>122</sup> *Id.*

<sup>123</sup> Andrew Parker & Adrian Michaels, *Financial Regulators to Strengthen Collaboration*, FIN. TIMES, May 26, 2004.

<sup>124</sup> *Id.*

<sup>125</sup> Lannoo, *supra* note 113 at 355.

<sup>126</sup> *See id.*

<sup>127</sup> *See id.*

<sup>128</sup> *See* Wei, *supra* note 11 at 266.

counting. The IASB provided that derivatives could be valued at the fair value, barring some limitations.<sup>129</sup> However, the European Commission did not believe that the IASB's methods for derivative accounting were correct, so the EU adopted a modified version of IAS 39 that contained differences to that of IAS 39 created by the IASB.<sup>130</sup> Because the EU does not apply the same variation of IAS 39 as other countries using international accounting standards, derivative accounting will not be uniformly applied when creating financial statements.<sup>131</sup> Ultimately, the harmonization process is undermined by this lack of enforcement.<sup>132</sup>

A final example involves Japanese companies that issued some of their bonds on several of the EU's exchanges.<sup>133</sup> The Japanese companies insisted that they be allowed to delist from the exchanges if they were required to either prepare their financial statements using IFRS, or reconcile the statements to IFRS.<sup>134</sup> Allowing financial statements not in compliance with IFRS defeats the goals of creating one set of internationally accepted standards.<sup>135</sup>

Another problem with the harmonization process is that the countries that are adopting international accounting standards will likely either have a veto option or the option to enforce only some aspects of the IFRS.<sup>136</sup> If countries opt to veto the requirement or choose selective enforcement, the comparability aspect of harmonization is severely harmed.<sup>137</sup> If the international accounting standard is not followed, the standard becomes "meaningless."<sup>138</sup> A regulatory body will help assist the compliance.<sup>139</sup>

Additionally, without an overarching international regulatory body, penalties and sanctions for violations of the international account-

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<sup>129</sup> *Id.*

<sup>130</sup> *Id.*

<sup>131</sup> *See id.*

<sup>132</sup> *See* Lannoo, *supra* note 113.

<sup>133</sup> Felicia H. Kung, *The Regulation of Corporate Bond Offerings: A Comparative Analysis*, 26 U. PA. J. INT'L ECON. L. 409, 427 (Fall, 2005).

<sup>134</sup> *Id.*

<sup>135</sup> *See* Osborn, *supra* note 6.

<sup>136</sup> Whittington, *supra* note 74 at 132.

<sup>137</sup> *Id.*

<sup>138</sup> Markus Ehrmann, *Procedures of Compliance Control in International Environmental Treaties*, 13 COLO. J. INT'L ENVTL. L. & POL'Y 337, 337 (Summer, 2002).

<sup>139</sup> *See* King, *supra* note 1 at 242.

ing standards may not be applied evenly from country to country.<sup>140</sup> For instance, the Commission established by the EU to assist with compliance and enforcement with the international accounting standards recognizes that “it may be difficult to harmonize sanctions due to differences in judicial and legal systems.”<sup>141</sup> An international regulatory agency will not have to worry about the differences in legal systems because it is a third party dispute resolution system.<sup>142</sup> An international regulatory agency would work outside of the individual nation’s legal systems and would be able to uniformly apply its sanctions across the globe.<sup>143</sup>

### III. THE SOLUTION

This section proposes the creation of an international accounting regulatory body to ensure the uniform application of international accounting standards. In doing so, the section will compare the body with other international regulatory agencies as well as with the SEC to describe its scope.

#### A. PROPOSAL

The harmonization of international accounting standards will have a tremendous impact on the efficiency of global business.<sup>144</sup> However, to deal with enforcement issues that loom over the entire process, an international regulatory body needs to be created to ensure that countries and companies alike are complying with the standards.<sup>145</sup> International regulatory agencies are used to accomplish goals that cannot be accomplished on the domestic level.<sup>146</sup> In this case, the regulatory agency would be used to address the accounting standard enforcement un-

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<sup>140</sup> See Thomas C. Pearson, *Creating Accountability: Increased Legal Status of Accounting and Auditing Authorities in the Global Capital Markets (U.S. and E.U.)*, 31 N.C.J. INT’L L. & COM. REG. 65, 127 (Fall, 2005).

<sup>141</sup> *Id.*

<sup>142</sup> See Graeme B. Dinwoodie, *A New Copyright Order: Why National Courts Should Create Global Norms*, 149 U. PA. L. REV. 469, 495 (December, 2000).

<sup>143</sup> See *id.*

<sup>144</sup> Osborn, *supra* note 6.

<sup>145</sup> Franck, *supra* note 10.

<sup>146</sup> Jonathan R. Macey, *Regulatory Globalization As a Response to Regulatory Competition*, 52 EMORY L.J. 1353, 1373 (Summer, 2003).



iformity problem, a problem which has not been solved domestically.<sup>147</sup> In fact, some U.S. business organizations are in support of the creation of enforcement standards, similar to the SEC's enforcement in the U.S., to keep the international capital markets strong.<sup>148</sup>

The proposed enforcement agency should have the same enforcement power of the SEC, but it would operate on an international stage, like other international regulatory agencies such as the Kimberly Process, the World Trade Organization, and the International Labor Organization. The international accounting regulatory agency would have power similar to that the SEC has on the national level.

### B. COMPARISON TO THE SEC

The SEC requires companies performing business within the United States to register with it.<sup>149</sup> Much like the SEC, the regulatory body would require all publicly traded companies performing business on an international scale to register with it. The purpose of companies registering with the SEC is to provide investors with relevant financial information so that the investors can make informed investment decisions.<sup>150</sup> Even though the SEC does not guarantee the accuracy of financial information, it does provide investors recovery rights if they can show that there was inaccurate or incomplete information provided by the companies.<sup>151</sup> Recent accounting fraud scandals, such as Enron and WorldCom, have led the SEC to gain a greater regulatory authority to protect the shareholders.<sup>152</sup> The international accounting standards were put into place to provide comparable and transparent financial statements for investors, the same reason companies are required to register with the SEC.<sup>153</sup> Likewise, the international accounting regulatory agency would be put into place to crack down on incomplete and inaccurate financial statements.

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<sup>147</sup> See Black, *supra* note 118, at 824.

<sup>148</sup> John C. Coates IV, *Private vs. Political Choice of Securities Regulation: A Political Cost/Benefit Analysis*, 41 VA. J. INT'L L. 531, 539 (Spring, 2001).

<sup>149</sup> Norris, *supra* note 79.

<sup>150</sup> Sec.gov, *The Laws That Govern the Securities Industry*, <http://www.sec.gov/about/laws.shtml> (Last visited Nov. 15, 2007).

<sup>151</sup> *Id.*

<sup>152</sup> Carl W. Mills, *Breach of Fiduciary Duty as Securities Fraud: SEC v. Chancellor Corp.*, 10 Fordham J. Corp. & Fin. L. 439 (2005).

<sup>153</sup> Zarb, *supra* note 2.

Registering with the international accounting regulatory agency is not going to be the only step in the process. Companies should also submit annual reports to the agency. The annual reports will be similar to the 10-K report required by the SEC in terms of content, which means there will be a section for financial statements.<sup>154</sup> With companies' financial statements, the international accounting regulatory agency can examine the accounting used by each company and determine if the company followed the proper international accounting standards.

Finally, to be an effective enforcement agency, the international accounting regulatory agency would have the power to impose penalties. Since the violators of the international accounting standards would be multinational companies, the most appropriate penalty would be in the form of monetary sanctions. These sanctions and any other penalties that the enforcement agency would implement would eliminate the need for incentives for individual nations to enforce the standards on their own. The incentives would not need to be present because the individual nations will no longer be charged with enforcing the international accounting standards.

### **C. THE ESTABLISHMENT OF AN INTERNATIONAL ACCOUNTING REGULATORY AGENCY**

An international accounting regulatory agency would be created through a treaty signed by the member nations of the IOSCO and IASB. The treaty would require the member nations to appoint one representative to the agency. The treaty itself would not have too many obligations for the member nations and it would simply address the overall concern of enforcing the international accounting standards. Because there would not be concrete obligations or specific duties by the signing nations, the treaty would more likely be signed.<sup>155</sup> The treaty might also be more likely to be signed because it might create good publicity for those nations signing it, indicating their support of efforts to curb securities fraud.<sup>156</sup> The agency, SEC-esque in nature, would be operating on a

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<sup>154</sup> Sec.gov, *United States Securities and Exchange Commission Form 10-K*, <http://www.sec.gov/about/forms/form10-k.pdf> (Last visited Nov. 15, 2007).

<sup>155</sup> *Developments in the Law—International Environmental Law*, 104 HARV. L. REV. 1550, 1555 (May 1991).

<sup>156</sup> *See id.*

global scale. The next section will propose how the new agency would address the problems faced by other international regulatory agencies.

#### D. THE COMPARISON TO OTHER INTERNATIONAL REGULATORY AGENCIES

To effectively solve the problem of lack of enforcement, an international agency must be created to enforce compliance.<sup>157</sup> Several international organizations are useful models in developing the international agency to enforce the harmonization process. Chief among these agencies are the SEC, the Kimberly Process, and the WTO. This section considers the best aspects of each organization to determine how the international accounting agency would operate.

The Kimberley Process is one example of a regulatory action that is on an international stage.<sup>158</sup> The Kimberley Process is a regulatory action created by the United Nations to monitor the import and export of diamonds to ensure that they are not from a “conflict area,” and to prevent sales of uncut diamonds to go towards funding rebel groups.<sup>159</sup> The Kimberley Process Certification Scheme (KPCS) summarizes the ways in which the trade of diamonds is supposed to be regulated by countries.<sup>160</sup> Under KPCS, a country must enact proper legislation, import and export internal controls, as well as provide transparent information regarding the diamond trade.<sup>161</sup> Those countries that participate in the Kimberley Process “can only legally trade with other participants who have also met the minimum requirements of the scheme and international shipments of rough diamonds must be accompanied by a KP certificate guaranteeing they are conflict-free.”<sup>162</sup>

However, just like the current situation for international accounting standards, the KPCS lacks proper enforcement. The burden falls on

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<sup>157</sup> See Franck, *supra* note 10.

<sup>158</sup> Margo Kaplan, *Carats and Sticks: Pursuing War and Peace Through the Diamond Trade*, 35 N.Y.U. J. INT'L L. & POL. 559, 587 (Spring 2003).

<sup>159</sup> *Id.*; *Russian Metals Giant Proposes Tracking Platinum-Group Metals*, RIA NOVOSTI, October 3, 2007.

<sup>160</sup> kimberleyprocess.com, Background, [http://www.kimberleyprocess.com/index.php?option=com\\_content&task=blogcategory&id=14&Itemid=26](http://www.kimberleyprocess.com/index.php?option=com_content&task=blogcategory&id=14&Itemid=26) (last visited Nov. 14, 2007).

<sup>161</sup> *Id.*

<sup>162</sup> *Id.*

the individual nations to monitor their compliance with KPCS.<sup>163</sup> For instance, in 2006, the Government Accountability Office (GAO) found weaknesses in the United States' implementation of the Kimberley Process through the Clean Diamond Trade Act.<sup>164</sup> Some of the areas of concern included the initial inspection process as the diamonds entered the country and the system that reports the receipt of rough diamonds with other participants.<sup>165</sup> Yet, the internationally accepted KPCS and the Kimberley Process have flaws that would not be found in the international accounting regulatory agency.<sup>166</sup> One such flaw is that it relies upon internal controls of nations from which "conflict diamonds originate."<sup>167</sup> Specifically, there is a lack of control over the mining activities, which allows the conflict diamonds to slip into the stream of commerce.<sup>168</sup> Since few diamond miners are licensed diamond dealers rarely check to ensure they are buying from legitimate exporters.<sup>169</sup> The lack of verification allows conflict diamonds into the market.<sup>170</sup> The purpose of international accounting standards is not to regulate the importing/exporting of a good; the purpose is to provide a set of standards for the creation of uniform financial statements.<sup>171</sup> Under the international accounting regulation agency, the companies doing international business would be registered with the agency, and they would be required to make annual reports. By requiring mandatory annual reports and imposing monetary sanctions for failure to comply with the standards, the international accounting regulatory agency would help eliminate the discrepancies in following international accounting standards like the SEC does with U.S. GAAP.

Another flaw of the Kimberly Process is the difficulty in defining conflict diamonds.<sup>172</sup> During the development of the KPCS, the definition of conflict diamonds changed multiple times.<sup>173</sup> Unlike the chang-

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<sup>163</sup> Kaplan, *supra* note 158 at 585; see *UN Security Council Renews Arms, Travel Bans for Further Year, Unanimously Adopting Resolution 1792*, STATES NEWS SERVICE, December 19, 2007.

<sup>164</sup> National-Jeweler.com, *U.S. Government Acts Quickly on Kimberley Process Critique*, [http://www.nationaljewelernetwork.com/njn/content\\_display/diamonds/e3iYElqmjoEm4u41hvo dsNTBA%3D%3D](http://www.nationaljewelernetwork.com/njn/content_display/diamonds/e3iYElqmjoEm4u41hvo dsNTBA%3D%3D), (last visited Jan. 3, 2009).

<sup>165</sup> *Id.*

<sup>166</sup> See Kaplan, *supra* note 158 at 561 and 586.

<sup>167</sup> *Id.* at 561.

<sup>168</sup> *Id.* at 601.

<sup>169</sup> *Id.*

<sup>170</sup> *Id.*

<sup>171</sup> Zarb, *supra* note 2.

<sup>172</sup> Kaplan, *supra* note 158 at 586.

<sup>173</sup> *Id.* at 594.

ing definition of conflict diamonds, the international accounting language has not changed throughout the harmonization process because the IASs that were created by the IASC are still in use by the IASB.<sup>174</sup> For instance, IAS 18 (Revenue) was published by the IASC in 1982.<sup>175</sup> In 1993, the IASC conducted a revision of IAS 18, and since then, there has not been another revision to the standard.<sup>176</sup> So in twenty-five years, the accounting standard for the treatment of revenue has gone through one change.<sup>177</sup> On the other hand, the Kimberley Process's definition of conflict diamonds changed multiple times since the creation of the process in 2002.<sup>178</sup> In fact, there are arguably two different definitions of conflict diamonds in use right now, and those may not adequately describe all the different conflicts that diamonds fuel.<sup>179</sup> In creating an international accounting regulatory agency, most of the standards it would be enforcing would have been created at least twelve years before the KPCS, and the standards have remained more constant than the definitions used in the KPCS.<sup>180</sup>

Another international regulatory agency is the World Trade Organization (WTO). The WTO was formed on April 15, 1994, becoming an effective agency starting on January 1, 1995.<sup>181</sup> The creation of the WTO arose out of the weaknesses of enforcement provided by the General Agreement on Tariffs and Trade (GATT).<sup>182</sup> The WTO created agreements which were discussed and ratified by most of the "world's trading nations."<sup>183</sup> These agreements provide the legal framework for international trade and commerce.<sup>184</sup> In addition to creating these agreements and trade guidelines, the WTO also settles disputes involving trade conflicts.<sup>185</sup> The WTO operates in an impartial manner when settling

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<sup>174</sup> Hanson, *supra* note 36 at 521.

<sup>175</sup> Iasplus.com, *Chronology of the IASC and the IASB*, <http://www.iasplus.com/restruct/chrono.htm> (Last visited Nov. 15, 2007).

<sup>176</sup> *Id.*

<sup>177</sup> *Id.*

<sup>178</sup> Kaplan, *supra* note 158 at 594.

<sup>179</sup> *Id.* at 595.

<sup>180</sup> See Iasplus.com, *supra* note 175; see Kimberleyprocess.com, *supra* note 160.

<sup>181</sup> WTO.org, *Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations*, [http://www.wto.org/english/docs\\_e/legal\\_e/03-fa.pdf](http://www.wto.org/english/docs_e/legal_e/03-fa.pdf) (Last visited Nov. 15, 2007).

<sup>182</sup> Carol J. Miller & Jennifer L. Croston, *WTO Scrutiny v. Environmental Objectives: Assessment of the International Dolphin Conservation Program Act*, 37 AM. BUS. L.J. 73, 80 (Fall, 1999).

<sup>183</sup> WTO.org, *What Is the World Trade Organization?*, [http://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/fact1\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact1_e.htm) (Last visited Nov. 16, 2007).

<sup>184</sup> *Id.*

<sup>185</sup> *Id.*

these trade disputes because “[t]he most harmonious way to settle these differences is through some neutral procedure based on an agreed legal foundation.”<sup>186</sup> There are, however, weaknesses in the WTO’s enforcement procedures.<sup>187</sup> One criticism is that the enforcement provisions are too broad and it is difficult for arbiters to determine the violations of the international law.<sup>188</sup>

Like the WTO, an international accounting regulatory agency would provide neutral procedures, based on an agreed upon foundation, for implementing sanctions against companies failing to comply with the IFRS. The agency would have in place penalties and sanctions that would be agreed upon by the representatives. The accounting regulatory agency would also address the weakness in the WTO’s enforcement mechanism. The problem with the WTO’s enforcement is the ambiguity of the enforcement provisions.<sup>189</sup> That problem does not exist with the international accounting standards because they are specific in nature, and the enforcement procedures would be specific as well.

A final international organization to compare with the accounting enforcement agency is the International Labor Organization (ILO). The ILO was established in 1919, and it became the “first specialized agency of the UN in 1946.”<sup>190</sup> The purpose of the ILO is to monitor international labor standards.<sup>191</sup> The ILO tries to ensure its labor standards are followed by member nations.<sup>192</sup> One major criticism of the ILO is that the body does not have enough power to ensure compliance with the standards.<sup>193</sup> The ILO does not have sanctioning power and it relies on “the power of persistent persuasion and the mobilization of shame against governments that fail to live up to the obligations they have voluntarily undertaken.”<sup>194</sup>

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<sup>186</sup> *Id.*

<sup>187</sup> J.H. Reichman & David Lange, *Bargaining Around the TRIPS Agreement: The Case for Ongoing Public-Private Initiatives to Facilitate Worldwide Intellectual Property Transactions*, 9 DUKE J. COMP. & INT’L L. 11, 35 (Fall 1998).

<sup>188</sup> *Id.*

<sup>189</sup> *Id.*

<sup>190</sup> ILO.org, *About the ILO*, [http://www.ilo.org/global/About\\_the\\_ILO/lang—en/index.htm](http://www.ilo.org/global/About_the_ILO/lang—en/index.htm) (last visited Jan. 2, 2008).

<sup>191</sup> *See id.*

<sup>192</sup> *Id.*

<sup>193</sup> James Mercury & Bryan Schwartz, *Creating the Free Trade Area of the Americas: Linking Labour, the Environment, and Human Rights to the FTAA*, 1 *Asper Rev. Int’l Bus. & Trade L.* 37, 46 (2001).

<sup>194</sup> *Id.*

The international accounting enforcement agency would address the criticisms that the ILO faces. The purpose of creating an accounting enforcement agency is to ensure compliance with the international accounting standards. To ensure this compliance, the enforcement agency would have the power to issue penalties and sanctions upon companies that violate the international accounting standards.

The proposed international accounting regulatory agency addresses many of the criticisms expressed towards other international agencies. Not only does the agency address the criticisms, but it also would be set up in such a way that it answers them positively. The next section addresses the one concern with all international organizations: state sovereignty.

#### **E. ARGUMENT AGAINST THE USE OF AN INTERNATIONAL REGULATORY BODY**

One argument against the creation of an international accounting enforcement agency is that it would conflict with state sovereignty.<sup>195</sup> State sovereignty has been interpreted to mean “that nation-states should have lawful control over their territories, to the exclusion of all others, and also that nation-states shall be able to control those territories and apply the law in those geographic areas.”<sup>196</sup> There is a view that “enforcement of international norms by international agencies should be subsidiary to that of national systems.”<sup>197</sup> One of the important aspects of sovereignty is that the nations are held accountable by its citizens.<sup>198</sup> International agencies have very little accountability compared to domestic agencies such as those found in the U.S where officials must be confirmed by the Senate.<sup>199</sup> In the international labor system, an international agency with enforcement power probably would not be tolerated because that agency would be punishing sovereign governments.<sup>200</sup>

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<sup>195</sup> *Developments in the Law—International Environmental Law*, 104 HARV. L. REV. 1550, 1565 (May 2001).

<sup>196</sup> Joseph F. St. Cyr, *The International Jurisprudence and Politics of Hazardous Substances: Managing a Global Dilemma*, 12 BUFF. ENV'T'L. L.J. 91, 104 (Fall 2004).

<sup>197</sup> Maurice Copithorne, *Briefer Notice: International Human Rights Law. Use in Canadian Charter of Human Rights and Freedoms Litigation*, 90 A.J.I.L. 181, 182, (January 1996).

<sup>198</sup> Terry L. Anderson & J. Bishop Grewell, *It Isn't Easy Being Green: Environmental Policy Implications for Foreign Policy, International Law, and Sovereignty*, 2 CHI. J. INT'L L. 427, 436 (Fall, 2001).

<sup>199</sup> *Id.*

<sup>200</sup> *Id.*

The international accounting regulatory agency would address the sovereignty concern by requiring all countries that have adopted the international accounting standards to appoint a representative to the agency. This way, there will be some form of accountability for the agency to each of its member nations because the nations themselves will have a say in who is a part of it.<sup>201</sup> The treaty that would be used to establish the agency would also help with the sovereignty issue by giving the agency accounting “legitimacy and expertise” because the members of the agency could train national officials on the international accounting field.<sup>202</sup> The sovereignty argument could be countered another way as well. Because the treaty does not really create any substantial obligations or duties, it does not tread on state sovereignty.<sup>203</sup> Likewise, the international accounting regulatory agency would not be punishing a sovereign nation for failing to comply with the international accounting standards. The agency would be penalizing individual companies and enforcing the standards against them, and not the countries. As with the criticisms facing individual international agencies, the accounting regulatory agency rebuts the concerns regarding its intrusion on state sovereignty.

## CONCLUSION

The globalization of business is causing companies to become more reliant on markets around the world.<sup>204</sup> As such, if all multinational companies apply the same set of accounting standards when creating their financial statements, the statements will be more transparent and will save costs for both investors and the companies themselves.<sup>205</sup> Cost savings and transparency are the two goals of the process of harmonization of international accounting standards.<sup>206</sup> The harmonization process has been successful so far, but there is one major flaw: there is no global enforcement mechanism, which would provide more legitimacy to the

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<sup>201</sup> See Anderson, *supra* note 198.

<sup>202</sup> See Farah Khakee, *The North American Free Trade Agreement: The Need to Protect Transboundary Water Resources*, 16 FORDHAM INT'L L.J. 848, 890 (1993).

<sup>203</sup> *International Environmental Law*, *supra* note 155.

<sup>204</sup> Linda Hanson, *Service Assesses Impacts of Pandemics on Business*, Dec. 7, 2007.

<sup>205</sup> Katharina Pistor, *The Standardization of Law and Its Effect on Developing Economies*, 50 AM. J. COMP. L. 97, 105 (Winter, 2002).

<sup>206</sup> Osborn, *supra* note 6.



process.<sup>207</sup> Without an international agency, enforcement is left to each individual nation.<sup>208</sup> Not only has this led to skepticism about the uniformity of enforcement, but it has also led actual enforcement discrepancies.<sup>209</sup>

The proposed enforcement agency would help ensure compliance with the international accounting standards.<sup>210</sup> It would also address the current criticisms of the enforcement process. The criticism regarding the lack of incentives would be answered because the enforcement function would be handled by an independent agency. This would eliminate the need to provide incentives for the individual countries since they would not be performing the enforcement. The proposed agency would operate in a similar manner as the SEC, only on an international level. Though there have been arguments against international agencies because of state sovereignty issues, the proposed agency would address that concern by including a representative from each member nation. The enforcement agency would also address the weaknesses and criticisms that are directed towards other globally accepted international agencies. With an international enforcement agency in place, the goals of accounting harmonization will be achieved, thus allowing the international business world to run more smoothly.

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<sup>207</sup> Franck, *supra* note 10.

<sup>208</sup> Whittington, *supra* note 74, at 132.

<sup>209</sup> Enriques, *supra* note 118, at 824; *see* Lannoo, *supra* note 113, at 355; *see* Wei, *supra* note 11, at 266.

<sup>210</sup> *Id.*