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GAAP AND IFRS: The convergence phenomenon

by

Paul Ryder Walter III

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of the requirements for University Honors Scholars

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DEDICATION PAGE

To my wonderful, beautiful, smart, and amazing fiancée, Alissa.

Thank you for all the hours of hard work and dedication you've put in to make this thesis possible.

-Much love

ABSTRACT

The past few decades have birthed dialogue regarding the convergence of U.S. and international accounting standards. With over a hundred countries using International Financial Reporting Standards (IFRS), it becomes natural to notice the purple elephant in the room in that a set of different principles serve as guide to accounting in the U.S. and for U.S. companies known as Generally Accepted Accounting Principles (GAAP). Some see it as simply a matter of time before a convergence of sorts takes place more completely between the two accounting rule frameworks. A look at GAAP and IFRS reveals some fundamental differences produced by the two ways of accounting. Proponents of convergence see these differences as a gap of sorts that should be narrowed to accelerate progress toward convergence. Opponents argue that substantial time and resources would be needed to necessitate convergence, and furthermore, that GAAP rules are superior and more appropriate than many international standards. This thesis aims to present logical and contextualized viewpoints on whether or not the convergence process should continue. It examines both GAAP and IFRS, and presents some differences, brief history, and theories that relate to both accounting frameworks and why or why not convergence should take place.

Keywords: convergence, IFRS, GAAP, standards, framework

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INTRODUCTION

What if accounting was more than just a major in college? What if an accountant was more than the stereotyped social outcast dedicated to bean counting? While these conjectures might occasionally turn out to be the case, the truth of the matter is that accounting affects each and every individual on a daily basis, and has potential to keep companies running smoothly and transparently, or in a corrupt manner with dire consequences for many. With that said, the mantle of being an accountant implies great responsibility. Competency is a necessity in the accounting field, and unquestionable ethics must be an ever-present reality.

Accounting is the language of business. It has the objective of conveying financial information to users who can use it to effectively aid in making decisions. College basketball fanatics utilize various statistics to pick that perfect March Madness bracket. Likewise, people can use financial information to make informed decisions that lead to financial success. Large companies often rely on raising capital from investors. Investors need accurate information to make decisions of where and how much to invest. This information is in the form of financial statements and other disclosures. Financial information isn't just important in aiding investors' decisions, but serves key roles in providing information to other types of users. Creditors need reliable financial information to determine whether to extend credit to various people or entities. Employees may be interested to see where the company they work for stands financially. Likewise, customers may have the same curiosity. Whatever the reason may be, many types of users utilize financial information in order to aid in making informed decisions. Accounting is the system used to produce the information, and accountants track data and generate the information.

Financial information isn't merely important for public reporting purposes. People within companies look to financial information to assess progress, lay out budgets, measure performance, determine financial capacity, and assess many other elements crucial to making decisions within the organization. This information derives from the process known as managerial accounting, in which the main objective is to provide management with information relevant to decision making. Given this objective, with the target users being managers within companies, few rules exist as to how accounting is to be executed exactly. Hence, there is no all-inclusive set of guidelines for managerial accounting. Financial reporting to the public, however, is a completely different story.

Three important elements of financial reporting for public purposes are ethics, understandability, and consistency. Ethics should ideally be the foundation on which all accounting is built. Without ethics, dishonestly has potential to quickly spring up due to greed, and financial information produced becomes useless, thus voiding any need to even keep reporting financial dealings. A second element of financial information is that it must be understandable. Like the need for ethics, understandability is essential in accounting. Users should be able to comprehend financial statements, and that comprehension and understanding is what translates into useful ammunition to execute effective decisions. Another core element of financial reporting is consistency. While ethics is non-negotiable, and understandability is key in the decision-making process, consistency is what allows for comparison between organizations. If companies report financial information in the same format and with the same calculations, it becomes possible for users to compare the financial dealings from different companies, and make decisions as to which to invest in, or in the case of creditors, which to lend to. Also, comparability complements the understandability element, as it provides a framework and basis through which to view and comprehend financial information. These elements make up the ideal characteristics that should be present in financial information. While they can be discussed, believed in, and thought through, it isn't enough simply to have generalized implied objectives. That is why accounting frameworks have emerged.

In recent decades, particularly in the twenty first century, dialogue has sprung up regarding the possibility of U.S. GAAP converging with IFRS and coming closer to fully adopting IFRS. This could mean that the SEC would start allowing companies to use IFRS for their accounting and financial reporting in addition to or as a replacement for U.S. GAAP. While outright adoption may not occur, convergence could potentially be viable.

Given this idea about a possible convergence, natural questions arise about how the two frameworks of IFRS and GAAP differ and how they are similar. There are certainly ways in which the two sets of standards differ. Some of these differences are more macro-level in nature. Those deal with big-picture ways that the frameworks have differing objectives and tactics used to achieve them. Other differences are more technical in nature, such as what methods are used to value assets, or specific rules relating to concepts such as revenue recognition. All in all, there are several major differences, and a plethora of smaller ones, all of which have to be thought through when assessing the viability of convergence.

Before delving into what these differences are, however, a step back needs to be taken. The question should be asked about why to push for convergence in the first place. There may appear to be some obvious reasons why convergence between IFRS and GAAP has been brought up as a possibility. Perhaps the most notable advantage relating to convergence lies in the unifying effect of allowing U.S. companies to use international principles. Theoretically, this would enable easier comparison between financials of different companies in different countries.

Because the rules governing preparation and presentation of financials would be streamlined as a result of convergence, users would be able to relevantly compare more financial data from more companies much more easily and efficiently. This would reduce the time it would take anyone to effectively make comparisons, and in turn, quicken many decision-making processes, not only on a national level, but on a global one.

While increased comparability might be a convenient advantage of converging U.S. and international principals, convergence does have its potential disadvantages as well. One significant downside to changing U.S. GAAP to conform to IFRS is the cost of implementation. Critics of convergence argue that the cost in time and money to implement training for new accounting rules, and actual conversion would far exceed any benefits reaped by full convergence. In other words, they propose that the cost outweighs the advantages. Other critiques typical to the topic of convergence are related to strong preferences to the way GAAP poses its rules. Many generalities exist as to the differing core principles behind international standards versus U.S. ones. Often these differing principles are enough to make people reconsider any ideas of a convergence, since such a phenomenon might alter the ideas behind U.S. GAAP and the United States' ethos on accounting principles.

As further exploration of convergence continues in the review of literature, the pros and cons of GAAP and IFRS convergence will become evident. While many technical differences exist between the two frameworks, there are also larger and more macro-level implications to U.S. and international accounting standards convergence. What are some large-scale effects of globalization of accounting standards? If accounting standards become more globalized, what other aspects of the world economy will become universalized and what will be the effects of such mass standardization?

REVIEW OF LITERATURE

Many aspects of society are constantly changing and, in many cases, moving towards globalism. With the advent of the information revolution, many every-day activities can be accomplished whose effects surpass the confines of political borders. It takes a split-second to disseminate communications through email to almost anywhere in the world. With internet access, a live virtual meeting is possible across countries. Whether for personal or professional purposes, people in today's age have nearly instant access to information in different countries and parts of the world. Naturally, this increased international exposure serves to propagate an increasingly globalized atmosphere. One area of society in which globalism is becoming increasingly prominent is the business world. Many companies buy and sell products and services in more than one country. Countries such as China have become manufacturing powerhouses, while certain countries in the Middle East are key sources of oil. This specialization by country and region increases the necessity for international trade, as well as companies extending their reach across the globe.

One facet of the business world that very much affects globalism relates to accounting standards. As mentioned in the introduction, there has been discussion about GAAP and IFRS possibly converging. With such an internationally-acclimated business environment, it is only natural to take note of the fact that different countries abide by different accounting standards. Part of the appeal of converging the two biggest accounting standard frameworks lies in the enhanced comparability between different companies in different countries. However, one problem is that any discrepancies between the standards would have to be reconciled.

A look at the two frameworks is necessary to understand the differences in rules. Much research has been done to compare the two accounting standard frameworks. There are several differences between both sets of standards. These differences have made the process of converging the frameworks very slow at times, as many are quite consequential in nature. They range from specific technical ones to bigger-picture differences about the general gist of the frameworks. A look into the histories of both U.S. and international accounting standards is necessary in understanding the nuance of differences that exist between accounting standards made by both frameworks.

In 1933, President Franklin Roosevelt held office, and both houses of Congress were controlled by a Democrat majority. During this time, a piece of legislation known as The Securities Act of 1933 was drafted by Congress and signed by the president. This law established the Securities and Exchange Commission, or the SEC. According to their website, the SEC was put in place in order to “require that investors receive financial and other significant information concerning securities being offered for public sale” as well as to “prohibit deceit, misrepresentations, and other fraud in the sale of securities” (U.S. Securities and Exchange Commission, 2013). The preceding four years had brought chaos and destitution, with industrial production having cut in half, the stock market falling 28 percent, and 25 percent of banks failing. Spurred on by this Great Depression, The Securities Act of 1933 and the formation of the SEC were mechanisms designed to prevent misinformation and combat the economically disruptive symptoms of an uninformed public (U.S. Securities and Exchange Commission, 2013). The presumption behind such a law and creation of a regulatory body was that the public, armed with more information, would be better off in terms of being able to see real and transparent financial happenings of a given company before investing in it.

While the primary purpose of the SEC was to provide a platform for transparency in financial reporting, it was also given the authority to set the standards for financial reporting, and therefore was the ultimate authority on all such matters, as designated by Congress. In an article on notable developments in the accounting industry, Stephanie Moussalli lays out a timeline of the different bodies that made accounting rules for U.S. businesses (2005). One notable time was in 1936 when the term “generally accepted accounting principles” was coined by the American Institute of Accountants (2005, 1936 section). A substantial leap of progress towards standards came two years later, when the Committee on Accounting Procedures (CAP) became the first standard setting body for U.S. private companies (2005, 1938 section). Throughout the years, as standard-setting bodies changed, evolved, and succeeded one another, the SEC was the end-all authority behind all standards, and remains so to this day. The SEC simply outsources its authority to set accounting standards to these various organizations.

Today, the standard-setting body in the U.S. is the Financial Accounting Standards Board, otherwise known as FASB. FASB has put together a framework of these standards known as the Accounting Standards Codification (Moussali, 2005, 1953 section). Each rule in the codification is designed to guide businesses and set requirements on how accounting is to be carried out, what methods and processes should be used to account for various financial dealings, and all things financial reporting. In other words, these rules guide accountants on how to prepare, process, and present financial information. The fact that accounting rules exist at all necessitates the aforementioned mandate for ethics and character. Accountants should always work in accordance with applicable rules as well as the intentions behind the rules.

The rules contained in the Accounting Standards Codification are still known as Generally Accepted Accounting Principles, or GAAP. These rules serve as an instruction manual for how financial information is to be prepared, organized, presented, and disseminated. Furthermore, they provide guidance as to how to treat certain concepts and account for certain costs, revenues, or valuations in a relevant, timely, appropriate, and consistent way. If accounting standards were subjective from company to company, they would be virtually useless to external users, since information would not be comparable. Net income might mean one thing for one company and something totally different for another. Or one company may classify certain purchases as the acquisition of assets, while another company may expense such purchases.

While the Financial Accounting Standards board (FASB) dictates U.S. accounting standards, other countries have their own differing frameworks. One such prominent framework that has been adopted by over one hundred countries is the International Accounting Standards Board (IASB), and has rules known as International Financial Reporting Standards (IFRS). International Financial Reporting Standards were initially created in order to assist developing nations by having a set of accounting principles the given nation could use as a starting point for financial reporting to get everything up and running. "But as the business world became more global, regulators, investors, large companies and auditing firms began to realize the importance of having common standards in all areas of the financial reporting chain" (American Institute of CPAs, 2011, p. 2).

Ray Ball, graduate professor of accounting at University of Chicago, discusses the history, ideology, advantages, and disadvantages of all things IFRS in his article, "International Financial Reporting Standards (IFRS): Pros and Cons for Investors" (2006). The article starts by addressing a basic history of international accounting standards.

From 1973 to 2000, the international standard body was called the International Accounting Standards Committee, or IASC (Ball, 2006, p. 3). It was formed by several countries spanning the globe, and had the aim to "be a set of rules that ideally would apply equally to financial reporting by public companies worldwide” (2006, p. 3). These “rules” set by the AISC are known as International Accounting Standards or IAS. The International Accounting Standards Body (IASB) replaced the IASC in 2001 to become the international standard setting organization. The rules set by the IASC still apply, however, rules that the IASB sets are now called International Financial Reporting Standards (IFRS).

After explaining an overview of IFRS and a brief history behind it, Ball dives into some of the theoretical pros and cons of uniform accounting rules in general. Ball explains that common accounting methods are helpful and much needed by users of financial information (2006, p. 6). Perhaps the main reason methods of accounting are helpful is to be a reference point to people that are making decisions based off information produced in the accounting process. The article explains that while accounting standards are helpful, there is a law of diminishing returns in terms of how specific standards can be made (2006, p. 5). In other words, while it is helpful for standards to be objective and specific, they can only go so far in applying to every minute situation without becoming too costly to justify. The article goes on to point out the growth IFRS has experienced, with over 100 countries adopting them and others tweaking them and using IFRS as national accounting standards (2006, p. 5).

As the title suggests, a central theme of the article is about IFRS and what it means from the standpoint of investors. The first advantage IFRS poses for investors, Ball notes, is that “IFRS promise more accurate, comprehensive, and timely financial statement information” (2006, p. 15). Investors can obviously benefit from these qualitative characteristics. Accuracy is key for investors. Having misleadingly inaccurate information presented to the public could lead investors to invest at the wrong time, and with expectations that will not be met. Comprehensive information is also necessary for investors, as they might key off a piece of information included in more comprehensive elements of the financial statements and disclosures to make investing decisions. Timely information is what gives investors a successful edge. Investing is all about timing. With these three characteristics in place, IFRS provides a strong look for investors, allowing them to more freely and trustingly rely on available financial information.

The second advantage pointed out about IFRS for investors relates to the competency and opportunity of less experienced, non-professional investors. Ball states that “Improving financial reporting quality allows them to compete better with professionals, and hence reduces the risk they are trading with a better-informed professional” (2006, p. 15). Investors of all kinds, professional and nonprofessional, play a role in making up a robust economy. The “small investors” Ball talks about are also key players in providing capital to both small and large businesses (2006, p. 15). The article argues that IFRS facilitates a more even playing field that gives less experienced investors the opportunity to at least have access to strong, reliable financial information. This allows for every investor, professional or not, to add capital to businesses, causing those businesses to be well funded and have the capacity to grow and continue to hire people as well as produce and sell products correspondent to the needs and desires of consumers (2006, p. 6).

The third reason IFRS is such an advantage to investors is two-fold. Making accounting standards uniform across different nations “eliminate[s] many of the adjustments analysts historically have made in order to make companies’ financials more comparable internationally” (Ball, 2006, p. 15). This reality, Ball points out, saves loads of money for companies that compile financial data into databases for the use of investors (2006, p. 16).

A fourth advantage piggybacks on the fact that uniform standards internationally makes financial information more comparable. The reduced cost and time incorporated in having to adjust for different accounting standards between different frameworks makes the market more efficient (Ball, 2006, p. 3). With less costs and time adjusting for the sake of comparability, more time and resources are freed up to be invested in the market, thus growing it, and allowing for more timely and frequent investing.

The last main advantage the article lists for investors related to IFRS also relates to cross country transactions. IFRS facilitates more ease in transactions across different countries by “removing barriers to cross-border acquisitions and divestitures, which in theory will reward investors with increased takeover premiums” (Ball, 2006, p. 16). This, yet again, has to do with companies under uniform accounting standards being much more comparable to each other. The increased comparability reduces costs, increases efficiency, as well as ease with which companies in different countries can go through substantial transactions with. All of these factors help the economy and markets to run more efficiently, thus generating more growth and success for investors.

Even the name International Accounting Standards Board, and also International Financial Accounting Standards, seems to be a call to consolidating accounting standards into one framework, not for just one country, but for as many possible across the globe. Ball points out that while over 100 countries have adopted IFRS and the concepts are global in nature, the standards in actual practice come up against the reality that much actual authority still lies in local governments (2006, p. 49). Even if a country has adopted IFRS, in other words, it is impossible to determine what ways certain specific accounting concepts are being applied. Ball talks about certain requirements of IFRS and makes the point that not every country will look to follow IFRS with the same detail to the same degree (2006, p. 50). One country could read a rule one way, and require companies in that country to spend much time and money abiding by the rule. Meanwhile another country could brush aside the rule or simply allow companies to follow it minimally. While the theory behind international principles is strong, the implementation of what is supposed to be a cohesive set of uniform accounting standards still has the tendency to look very different depending on where it is practiced.

One particular area that Ball focuses on to support the point regarding differences in practice of IFRS is rules requiring companies to periodically reassess and revalue assets to fair value. He states that "The drift toward fair value accounting in IFRS will only accentuate the extent to which IFRS implementation depends on manager and auditor judgment" (2006, p. 32). In actuality, this accentuation that leads to dependence on managers and the like only adds to the fact that IFRS might not end up so uniform between different countries. Rules like the fair value rule necessitate judgment based on a principle, the principle being fair value, which is quite subjective in nature. This phenomenon substantiates the claim regarding international principles being quite principles-based. Principles-based rules from IFRS lead to more professional judgment having to be implemented. And when more of people's judgement is thrown into the equation, the application of accounting standards becomes far less uniform.

Taking a step back, what does it mean if the IFRS in practice is far less uniform? Well, the main and obvious advantage of uniform accounting standards is increased comparability. With rules in place that apply to many countries and not just one, accounting information can be accurately compared and contrasted by users. However, knowing that IFRS applied in actuality is far less uniform certainly raises concerns that go against the very tenants of making standards more comparable.

The result of hard and fast rules allows professionals to act in objective ways by a set of objective and specific rules. These rules, when applied to different companies, produce comparable products. For example, picture a rule that delineated that no matter what, assets are to always exist on the books at cost value. While there are different ways to account for the original cost of assets, this rule of always valuing assets at cost simplifies and standardizes the way firms would count assets on the balance sheet. This specificity allows for more efficient accounting practices, as professionals would need significantly less time to make certain determinations.

Having principles-based rules aims to give professionals leeway by strongly advising them to perform accounting procedures in line with certain values and characteristics. However, this leeway given isn't used the same way by different people, managers, governments, etc. In fact, it is much the opposite. Aside from the chance the principles are abused to allow misleading in financial reporting, much more incidental consequences exist to the principles-based approach. Every different entity will handle each rule or principle that is objective in nature in a different way. Perhaps this hinders one of the goals of IFRS of providing countries with a truly internationally uniform set of accounting standards that will cause information to be maximally comparable.

Hand in hand with the reality of differing accounting practices all within the guise of IFRS is the enforcement phenomenon. Ball describes the fact that although the International Accounting Standards Board (IASB) is the International Financial Accounting Standards setter, it has no authority to enforce the standards as rules, given that they are all used in different countries, each with its own sovereignty (2006, p. 35). He states that "Worldwide regulatory bodies generally are regarded as toothless watchdogs" (2006, p. 34). This is perhaps quite an apt way to describe the IASB. Rules that can't be enforced are a failure by nature. More desirable results are produced if accountants properly abide by standards. If the standards aren't enforced, which they are not, then there is no way to tell whether or not they are being applied properly at all.

One generality about U.S. and international standards is expanded on in a piece written by Doctors Oris Guillaume and Denel Pierre (2016). This study on literature describes IFRS and GAAP from a macro-level view, alleging that U.S. accounting standards tend to be more rules-based versus more principles-based international standards. The authors stipulate that massive-scale accounting scandals around the early 2000's are much of what led to this discussion and argument for more principles based accounting standards. Guillaume and Pierre further go on to say that

> Proponents of principles-based accounting standards argue that it focuses more on professional judgment, there are fewer rules to bypass, and it will more likely lead to an appropriate accounting treatment. However, opponents of the principles-based approach argue that the lack of detailed rules will even lead to more abuse. (2016, p. 64)

It's clear to see that there are credible arguments on both sides of the coin. On one hand, principles can direct accounting professionals in a more all-encompassing way to guide the spirit of the law, the goals of integrity behind accounting functions. On the other hand, however, specific rules can clear up confusion in the potential gray areas that could be present in a principles-based system of standards. Furthermore, rules might sometimes restrain professionals from questionable practices even if those professionals deem them adequate.

The article's purpose is to not only show these differences but to give an idea as to what the future holds for GAAP and its convergence with IFRS. A timeline is presented that lists different key steps in the convergence process such as the 2002 Norwalk agreement in which the IASB and FASB acknowledged "the joint commitment to developing high-quality, compatible accounting standards that could be used for both domestic and cross-border financial reporting" (Guillaume and Pierre, p. 65). The timeline goes on to list the 2005 plans of the Securities and Exchange Commission to release "a roadmap allowing IFRS filings without U.S. GAAP reconciliation for foreign firms by 2009 or earlier" (2016, p. 65).

Given this roadmap, as well as understanding the many differences that exist between GAAP and IFRS, the big question Guillaume and Pierre researched had to do with what the general gist was as of 2016 in the quest to bring the frameworks together. The conclusion from their research was that adoption would be difficult, as there are many differences between the standards, but still possible. Their findings were geared towards the realization that convergence might be a plausible way to fulfill the desire of many for one centralized system of accounting rules.

> While some feel that the topic of convergence will remain unresolved, others are optimistic about the idea of having one set of global accounting standards. Many argue that a single set of high-quality accounting standards will improve comparability, transparency, verifiability, value relevance, and understandability of financial information. They believe that the convergence will bring many challenges for corporations, investors, and accounting professionals, but it will present many opportunities for them. (2016, p. 71)

The convergence could potentially go the route of allowing for this centralization, while simultaneously letting the U.S. to have its own version so-to-speak of the converged set of rules. This is the middle of the road ideology that seems to be most relevant in today's academic study of converging frameworks.

The SEC roadmap release in 2005 and the Norwalk agreement are case and point to an assertion pointed out in an article by Mark Sullivan (2014). In it, referring to the Bush Administration years, Sullivan states, “there had been considerable momentum for the United States to adopt IFRS for publicly traded companies” (2014, para. 2). However, he did go on to mention that “Under the Obama Administration, this impetus appears to have dissipated” (2014, para. 2). Clearly, there has been a constant ebb and flow to progress in converging U.S. and international accounting standards. While there have been decisions made to further convergence, there hasn’t been consistent support of it all along.

Any consideration of convergence begs an evaluation of some of the nuts and bolts of IFRS and GAAP individually, and furthermore, the main differences between the two sets of standards. A 2009 article by William Bratton and Lawrence Cunningham provides information on these differences. (See Appendix)

One of these listed differences deals with departures from the standards. In certain circumstances, departures from both GAAP and IFRS are allowed (Bratton and Cunningham, p. 1008). However, per the AICPA Code of Professional Conduct, rule 204 explains that departures from GAAP are allowed but very rare. In other words, it is apparently more difficult to justify a departure from GAAP than any departure from international standards.

Another difference deals with restructuring costs and expense timing differences. For GAAP, restructuring costs are recognized when the costs are incurred. Under IFRS, restructuring costs are recognized when they are announced or commenced (Bratton and Cunningham, p. 1010). This difference perhaps adequately exemplifies that assertion made by Guillaume and Pierre regarding principles versus rules-based standards. The GAAP guidelines for restructuring costs clearly show that timing of an expense should be based on the hard and fast rule of when it is incurred (2009, p. 1017). This shows the clear-cut nature of U.S. standards. Meanwhile, with IFRS having a slightly different take on restructuring costs, it is clear to see the strategy taken in international rules. IFRS goes as far as to dictate that restructuring costs should be recognized when announced. In other words, international standards in this case are assuming the idea that if a cost is likely to be incurred, it should be recognized at the time of conjecture. IFRS demonstrates its principles-based approach by directing companies to recognize costs as plans are announced, and intentions are present, even before they technically are incurred.

Other differences between IFRS and GAAP exist regarding revenue recognition. For example, under GAAP, service contracts are to be "amortize[d] over service period without up-front recognition" (Bratton & Cunningham, 2009, p. 996). This would mean that revenue is generally recognized for the service contract in even increments over the life of the contract. While this is true for GAAP, IFRS differs slightly in that it "allows up-front recognition when partial performance has occurred" (2009, p. 1012). This is antithetical to the very premises that GAAP usually abides by. U.S. standards generally tend to lean toward a sort of matching principle in which revenue recognition is divided over the period it is earned rather than being counted at a different time.

Accounting for inventory is another area in which international standards differ from U.S. ones. GAAP allows for a variety of inventory accounting methods to be used including last-in-first-out (LIFO), first-in-first-out (FIFO), and others. IFRS prohibits the use of LIFO as an inventory accounting method. In an article by William White on the LIFO inventory method and its relationship to the convergence, the effects of having to switch away from LIFO are examined (2017). Basically, the last-in-first-out method or LIFO dictates that if a company buys products at different prices at different times, then the value of a widget that sells is the value of the most recent product that was purchased at a given price. For example, assuming all widgets are the exact same product, a company purchased one widget in January for $40, one in March for $42, and one in September for $45. In October, it sells one of those widgets, then the natural question arises on the cost basis of the widget. Under FIFO, the cost basis would have been $40, since it would count the value of the first widget in inventory. However, under LIFO, $45 would be the accounted for cost basis of the widget sold, since it counts the most recent widget put into inventory.

These differences between inventory methods can have a significant impact on a company's earnings. Assume per se that the widget sold in October was sold for $50. Consequently, under FIFO, the profit from the sale would be $10, while under the LIFO inventory method it would be just $5. Given that company's use LIFO would have to switch if brought under IFRS, it is vital to assess the consequences of such a phenomenon. The potential for higher earnings under FIFO in a rising cost environment might boost net income. However, while higher profits might appear as a positive, tax consequences must be considered. One article states that "Consequently, adoption of IFRS would cause all current LIFO reserves – amounting to billions of dollars – to immediately become taxable income" (King, 2008, p. 15).

The following is an excerpt from William White's article on "The LIFO Conundrum":

> A recent study performed at the Georgia Tech Financial Analysis Lab examined the tax effect, among other impacts, of changing from the LIFO valuation of inventory to FIFO. It revealed that 36% of US companies use LIFO in valuing all or a portion of their inventories. Further, the study reviewed a sample of 30 companies with the largest percentage of LIFO reserves to total assets, and found that their pretax income would be higher on average by 10% and 12% in 2006 and 2007, respectively, if they used FIFO in valuing their inventories. More importantly, the study revealed that these same companies would have more than US$15 billion of cumulative federal income taxes due if they switched from LIFO to FIFO. Under current IRS regulations, most of these companies would be allowed to spread their tax payments over four years. This seems

> fair and equitable at first glance, until one realizes the gravity of these tax payments. For example, Exxon Mobil Corporation had a LIFO reserve balance of US$25.4 billion at the end of its fiscal year 2007. At a 35% effective tax rate, the company would be forced to pay the IRS approximately US$2.2 billion a year for four years (approximately US$8.9 billion in total, or 4% of its total assets). (The Conundrum section, para. 2)

Given this reality about the jump in tax liability, this difference really makes the idea of convergence tough for U.S. companies that use LIFO. If convergence were to occur, there could potentially be plans, however, to ease the transition or to somehow compromise IFRS to better accommodate companies using LIFO.

Another key difference between the frameworks deals with asset valuation. In GAAP, cost basis is used, which means that the historic cost is how assets are valued on the balance sheet. "IFRS actually permits companies to write up the value of property, plant, and equipment assets above historical costs" (King, 2008, p. 16).

To illustrate the effect of these revaluations, assume that a widget is bought for $50. Cost basis would have $50 as the asset's book value for reporting purposes. However, under fair value method, the asset would be valued at whatever its fair market value is at the time of reporting. If that asset was revalued at $55 at the time of reporting, it would be recorded accordingly under the fair value method. Clearly, this difference can have a hugely material effect on a company's financials. A large corporation may have fixed assets and land that was purchased many decades before a given reporting period. Without adjusting for fair value the company may show these assets on the balance sheet as being worth small fractions of what they would be worth at the time of reporting. Being allowed to use the fair value method for valuation could change the company's balance sheet by immense amounts, and therefore have a significant effect on many important ratios investors use to make decisions and assess and compare financial statements.

This rule difference is case and point to the way IFRS utilizes blanket principles when determining accounting standards. In this case with asset valuation, IFRS guides companies to give a real-time financial snapshot on their balance sheets, that provides investors with a realistic view of the value of assets. But this attempt to make the balance sheet more accurate can have its caveats. First, the whole idea of a fair value for assets is subjective in nature. Alfred King's article titled "GAAP vs. IFRS: Will the Real Fair Value Please Stand Up?" (2008) describes the difference in the very definition of fair value that the International Accounting Standards Board (IASB) holds versus the United States' definition.

> The new definition of fair value differs from fair-market value in two critical areas. First, rather than dealing with an exchange between a 'willing buyer and willing seller,' as used in the fair-market value definition, fair value requires an exit approach. In other words, you only look to see what you could sell an asset for, even if you just bought it yesterday. (p. 14)

Fair value by its very nature is constantly changing, up to consumer demand, and measured by countless differing standards. The fact that differences in definition of the term "fair value" exist only accentuate such subjectivity. King further goes on to explain a potential downside of allowing revaluations for companies. "A possible negative for U.S. adoption of the revaluation model is that because valuation is inherently imprecise, some companies may take an aggressive approach, at least in the initial revaluation" (p. 16). This aggressive approach King talks about might mean that companies set the value of their assets significantly above what they may be worth, or at least very optimistically, thus skewing the balance sheet. The allowance of revaluations shows IFRS's tendency towards being principle oriented. However, GAAP offers much more clear-cut rules that don’t allow revaluations, and this avoids all the potential downsides that the IFRS allowances may pose. With the complexity of the IFRS principles about fair value and the option to revalue assets also would come costs of revaluing. Much time and money would be spent in revaluing should companies choose to do so, making it close to not worthwhile much of the time, given that the cost may outweigh the benefits.

One difference between GAAP and IFRS relates to accounting for construction. Often, the percentage of completion method is used to financially account for progress in construction processes and bill clients appropriately at the proper intervals. Like the name sounds, percentage of completion accounting for construction contracts essentially aims to even out revenue and expenses by using a certain proportion-based formula. When the percentage of completion cannot be determined IFRS requires the cost recovery method, but GAAP requires the completed contract method (Pacter, 2003, p. 68).

The cost recovery method is a very conservative method of accounting that deals with how and when to account for profits from sales. Under it, the seller only realizes gross profit once the entire cost of the good or service being sold is paid for by the proceeds of the transaction. In other words, each initial payment made by the buyer goes toward cost of goods sold. It’s only when the entire cost of goods sold is recovered through payments from the buyer that profit can start to be recognized. As pointed out in an article on the cost recovery method, “Realistically, its use calls into question why the seller is even doing business with the buyer” (“Cost Recovery Method,”, Overview section, para. 2). The reason for this calling into question is that under the cost recovery method, the seller treats each payment as reimbursement for the costs of goods or services, until it is fully paid for. And sometimes it wouldn’t be till later payments are made that the transaction would give the seller any particular benefit from an economic standpoint judging by the books.

As an example, suppose that Company A sells a widget that costs $8,000 to make for $10,000. The buyer is set to make payments of $1,000 per month. Under the cost recovery method, Company A would record the first eight payments as going against the cost of the widget. Then Company A would account for the gross profits of $2,000 as the last two payments were made. The cost recovery system essentially delays the recognition of profits. By necessitating the use of the cost recovery method when percentage of completion can't be figured, IFRS is taking a very conservative approach. While conservatism has been a tenant of GAAP for a long time, this method, in essence, goes against the concept that is often prevalent in GAAP of recognizing profits evenly and in accordance to when they are earned. This is known as the matching concept.

While IFRS mandates the use of the cost recovery method when percentage of completion can't be used for construction projects, GAAP mandates another method called completed contract. Although GAAP tends to lean heavily towards recognizing revenue evenly over the period it's earned, the completed contract method would be an example of where GAAP must veer from this principle. Like the cost recovery method, the completed contract method fails to distribute profits from a project over the period they are earned. Instead, the completed contract method has all costs capitalized during the project. It isn't till the end of a project that everything is expensed and revenue, and therefore also profits, are recognized ("Completed Contract Method,", para. 1).

Other differences between GAAP and IFRS lie in what is required to be publicly disclosed. For example, while IFRS requires "one year of comparative financial information", GAAP has no such requirement but lists comparative information as desirable (Pacter, 2003, p.

68). GAAP requires the reporting of total comprehensive income, while IFRS does not. Departures from standards are “covered by auditing and ethics rules” under GAAP while in IFRS they are simply “permitted in ‘extremely rare’ circumstances” (2003, p. 68). This vaguer guidance from IFRS is perhaps an instance of international standards simply leaving professionals with a principle, rather than a specific rule. Conversely GAAP does provide the specific guidance by directing professionals to a specific list of rules that determine what departures from the standards are appropriate and also when such departures are appropriate.

Given these differences, many scholars have set out to explain ways and reasons that convergence should move forward or should not. Many overarching themes emerge about the pros and cons of convergence. Some of the common themes relating to reasons for convergence are comparability, streamlined information, a centralized place to go for standards, and much more. Typical cons that are given usually relate to the cost of training professionals in the US for IFRS and the cost of implementing the convergence to one set of standards. Furthermore, there is disagreement on just about every rule that differs as to whether the GAAP rule is better than the way IFRS treats that same concept and vice versa. Consequently, these differences keep IFRS and GAAP a distance away from each other in terms of similarity.

One particular area of consequence which could potentially be heavily affected by any sort of convergence of accounting standards is taxes. While there are many book differences between U.S. and international standards, tax enters the equation and adds an entirely different dimension to what effects convergence could have. Earlier, the LIFO reserves dilemma was explained. However, convergence would still have many more ramifications for taxes than just ones related to inventory accounting methods. Jana Roe’s article titled “Transition from US GAAP to IFRS: Analysis of Impact on Income Tax Administration in USA” (2014) gives an overview of taxes and explains the relationship between tax accounting and book accounting.

Before delving into the details, Roe talks about the differing nature of tax reporting versus book. She also explains the relevance of tax and the prevalence of professional tax preparation, stating that “worldwide tax collections constitute the greatest source of demand for accounting services” (2014, p. 86). The introduction also mentions that taxes are the major source of income for governments. Roe then goes on to give an overview of the tax filing process from a conceptual standpoint. The following passage from her article specifically talks about preparing corporation tax returns.

> US domestic companies that prepare their financial statements per US GAAP compute their income tax using their accounting result modified by tax adjustments and report their computations on Form 1120, U.S. Corporation Income Tax Return and Schedule M-3, Net Income (Loss) Reconciliation for Corporations with Total Assets of $10 Million or More. (2014, p. 91-92)

In other words, the amount of taxes a corporation pays is the given tax rates multiplied by taxable income for that corporation. But to get to the taxable income figure, the corporation first reports its book income, then tax adjustments are made to get the book income to taxable income. GAAP denotes the U.S. standards for getting to book income. Tax preparers and CPA’s in the U.S., therefore, are trained in book/tax differences between GAAP book numbers and getting those to the IRS standard for taxable income. Allowing IFRS as an accepted method of accounting in the U.S. would have significant effects on the tax preparation industry. Many questions arise when dealing with IFRS and tax, such as the following:

- Will the IRS have to add code that specifically deals with IFRS book income and what adjustments to make to get to taxable income?

- Will book/tax adjustments for GAAP to IRS remain the same?
- In what ways will adjustments between GAAP to tax and IFRS to tax numbers differ?

These questions just scratch the surface of the dilemma facing the IRS and the tax profession at large. Major shifts would have to occur just to allow companies to only have to submit IFRS book accounting info for tax purposes. Even more major change would take place in the world of taxes if any sort of convergence were to occur. If such change were to occur, the IRC (Internal Revenue Code) could potentially need serious revision to accommodate the new rules.

After analyzing tax and its relationship to convergence, it seems that researchers are simply left with more questions. Roe's article goes on to address some of the natural concerns that arise and explains the current state of rules in the U.S. with regard to what kinds of reporting are allowed. "In 2007, the SEC allowed foreign corporations that prepare their financial statements using IFRS as formulated by the IASB to use those financials for SEC filing without reconciliation to US GAAP" (2014, p. 92). Roe goes on to explain, though, that "US domestic filers are still required to use US GAAP and are not permitted to use IFRS" (2014, p. 92). The IRS holds that companies that file U.S. federal taxes must have financials in GAAP first, and subsequently compute the book to tax differences based off the GAAP financials. However, the IRS has allowed worldwide consolidated net income to be calculated with IFRS as the starting point. That has been the exception since 2009 (Roe, 2014, p. 92). Clearly, progress is slow but there has been movement on the part of the SEC and the IRS to accommodate, at the very least, foreign companies, and U.S. companies with global reach.

The article goes on to talk about the plans for future progress of the convergence. Perhaps at some point a day will come when the IRS starts allowing IFRS prepared financials to be the starting point for tax preparation purposes. Given the fact that tax numbers must be sourced from financials, it is most important for professionals and the government to understand the effect of allowing IFRS to be a starting point. The article talks about this importance and lists effective measures that should be taken including training on IFRS and how it works for IRS personnel, technical advice, working with the community to identify concerns, developing procedures to address the different nuances of IFRS as opposed to GAAP, and possibly starting an IFRS group that become the experts on the system and can be go-to resources (Roe, 2014, p. 94). As it is, it takes years to learn even the current tax code and how to process GAAP derived book numbers. Adding another allowable accounting method for tax purposes would take years and much money to prepare the tax industry for.

Roe isn't the only one to point out the significant impact changing or converging to IFRS could have on tax. Christine Newell states that "converting financial statements from one reporting standard to another will have broad implications beyond just financial (book) accounting. Tax accounting and many other aspects of the company's operations will be affected" (2008, p. 335).

In her article titled "IFRS is Coming: What Does This Mean for Tax?", Newell discusses the vital necessity of tax preparation having a heightened awareness of IFRS and how it works (2008). She points out that preparers should understand the differences between U.S. and international standards so they can accordingly adjust how book/tax differences are made (2008, p. 335). Newell brings up several questions in relation to the idea of book methods changing. One of which is whether an accounting method change form might be needed if IFRS would be used as a starting point for calculating tax. There are a few types of accounting methods currently used and allowed as a starting point for tax prep, however IFRS would add an entirely new, comprehensive method, that would require much planning. This change in accounting methods form would potentially be only one minor change in a sea of big changes to how taxes are prepared. IFRS could mean a new set of book/tax differences. With current U.S. standards, an example of a common book/tax difference is for travel and entertainment expenses, half of which are not deductible, and are therefore accounted for in an M-1 entry which reconciles book net income to taxable income. If IFRS was allowed, preparers would need to know whether the same travel and entertainment book/tax difference is necessary. Furthermore, preparers might need to learn a slew of new adjustments that would need to regularly be made with IFRS numbers constituting the starting point.

William Stromsem, a Juris Doctor and CPA, wrote an article that starts off along the same vein of tax related matters and IFRS (2009). In it, Stromsem talks about the fact that because IFRS utilizes fair value rather than historical cost to determine the value of assets, financials might need to be revamped just for tax preparation purposes. Companies may have to prepare numerous Forms 3115, Application for Change in Accounting Method, to change tax accounting methods.

Stromsem's article was written at a time when the concept of convergence was alive and being talked about. The article mentioned a slowing in the process through an announcement by the SEC Chairman, Mary Shapiro (2009, p. 322). However, despite this, Stromsem clearly expresses a view that eventual convergence is inevitable.

As the title might hint, this article puts emphasis on the necessity of preparation on the part of tax practices for a convergence of standards. One of the assertions Stromsem makes in his article is that “IFRS also relies more on professional judgment than on strict accounting rules, so accountants will have to take more responsibility for evaluating tax-related issues in financial statements and in tax planning” (2009, p. 322). Clearly, Stromsem sees the principles-based elements of IFRS and in this article, is taking note that one implication of this is that more professional judgment will be required by accounting professionals. The increased reliance on professional judgment would likely change the nature of the accounting profession.

In today’s business world, different levels of professional work contain different levels of responsibility. Generally speaking, entry level work tends to lean more toward very objective processes. These processes usually require some training for an entrant with little or no experience. But this training prepares them adequately to work based on objective guidelines in place in the company. As employees become more skilled, they can be given greater responsibilities. Work goes from merely technical tasks to including more decision making. Managers and company leaders are generally at the rank where they have authority to make decisions and use professional judgment. Since IFRS is by nature principles-based, it implies a broad range of subjective decisions to be made regarding numerous accounting methods and procedures.

Some differences between IFRS in GAAP are related to the treatment of software development costs and LIFO. In relation to the software development costs differences, Newell cites various Internal Revenue Codes to show that “if these differences are not tracked correctly there is a high possibility of error, which may lead taxpayers to unknowingly report a different position than their historical tax method” (2008, p. 335).

With regards to LIFO, Newell presents an interesting dilemma. She shows that under IRS guidelines, if LIFO is going to be used to attain the ending inventory for tax purposes, then

LIFO must be the only method used by the company for any purposes (2008, p. 335). Since LIFO is currently disallowed by IFRS, this would essentially imply an all-or-nothing move to either disallow LIFO entirely for U.S. companies, or for IFRS to allow LIFO, should a convergence take effect.

Newell's big picture conclusion is two-fold. It surmises that if convergence were to move forward and take place on a massive scale, it would form more of a revised, global set of standards, that might look a little different form today's IFRS (2008, p. 336). Secondly, she stresses the importance of preparing managerially, and in every way for the apparent differences that might come about as a result of such a convergence (2008, p. 336).

Another article by John McGowan and Matt Wertheimer on the implications of the convergence for tax asserts that it isn't mere adoption of IFRS that is in the process of happening (2009). It lists several ways in which the differences are narrowing and both U.S. and international standards are forming rules that facilitate that merging. In other words, both sides are altering rules that would ease differences between the frameworks.

Given the proven vitality the idea of a convergence has on tax and how taxes are affected, McGowan and Wertheimer stress the importance that tax professionals make sure clients are set up for success. The importance of knowing the ins and outs of what convergence would entail is vital for many purposes. Professionals, McGowan argues, should be poised to set clients up for success by facilitating heightened awareness and the learning of IFRS, and different items that are relevant (2009, p. 843). This consulting and preparation on the tax end of everything is so important, as accounting under IFRS might affect tax treatment significantly, and consequently, affect a company's bottom line. What's stressed a great deal is not only education on IFRS and proposed changes for tax professionals, but also for clients to have preparation and to be taught the basics of it all (2009, p. 843). This would aid in the process of working on taxes, and knowing how this bottom line can be affected by all the differences in accounting method.

On a related note, the article surmises that systems must be developed to account for and facilitate GAAP and IFRS for tax preparation purposes. "To reflect the changes brought about by IFRS, companies could modify their accounting and reporting systems. Of immediate concern is the ability to capture parallel information on a U.S. GAAP and IFRS basis, especially for the year(s) immediately prior to adoption" (McGowan & Wertheimer, 2009, p. 844). The authors pose the vitality of these systems being put into effect. This is quite an obvious necessity, given that systems and software are an integral part of any large organization's accounting, whether for managerial purposes in private companies, reporting purposes for public ones, or even tax preparing public accounting firms.

International Accounting Standard 12 (IAS 12) focuses on income taxes, and so does its U.S. counterpart, Statement of Financial Accounting Standards number 109 (SFAS 109). An exposure draft was put out by the IASB in 2014 that was intended to amend IAS 12 to make certain aspects of accounting for income taxes under IFRS line up closer to U.S. standards. This draft addressed various tax issues such as book to tax differences, uncertain tax positions, and much more. (McGowan & Wertheimer, 2009, p. 844)

Given a look into systems needed to allow for more convergent standards that affect tax, and also the draft put out by the international sector for the accounting for income tax, it's clear to see tax's relevance in the conversation about convergence. This article most emphatically calls for recognition that standards could potentially change as both GAAP and IFRS find common ground and compromise to the middle. It vies for companies, tax preparers, individuals, and everyone else to assess and plan accordingly (McGowan & Wertheimer, 2009,

p. 848). Recognition should lead to training, and being ready is the best way to help ease any transition in the future, should it progress.

DISCUSSION

Many differing views exist around the idea of GAAP, IFRS, and the concept of convergence in general. Some say convergence should absolutely take place, while others hold quite the opposite view, arguing that accounting standards shouldn't be standardized on an international level. With so many details in play related to differences between GAAP and IFRS, the dissonance between viewpoints is only accentuated. Perhaps there are several assertions though that can be agreed upon more widely.

- GAAP and IFRS have differing rules for accounting methods and treatment of various transactions, financial statements, etc.
- GAAP and IFRS have different reporting requirements
- GAAP and IFRS have different backgrounds
- GAAP and IFRS come from different organizations
- GAAP and IFRS have different core purposes

The review of the literature provides guidance on just a few of the many substantial accounting method differences between the frameworks. These differences affect countless elements of business and accounting, from inventory valuation to financial statement presentation. Each difference further polarizes both GAAP and IFRS from each other, making the idea of convergence significantly more complicated and difficult. People's viewpoints fall on both sides of every single difference, which at the very least, makes any effort to converge much more time consuming. Convergence of the rules would have a very realizable affect, as accounting methods are what are used to produce information that is available to users.

GAAP and IFRS not only have inherently different accounting methods imbedded in their systems, but both differ significantly in what they require from a reporting standpoint. In some instances, for example, IFRS requires the reporting of prior year financials alongside current year, while GAAP doesn't require it. This is just one of the reporting requirement differences existent between U.S. and international standards. Different reporting requirements affect the part of accounting people see. The financial information people are given by companies is what they have to base decisions off of. Given this fact, it is vital that the information be succinct, meaningful to users, and conducive to interpretation for the purpose of decision making. GAAP and IFRS have numerous reporting requirement differences that would have to be reconciled to accommodate further convergence.

GAAP and IFRS not only differ in accounting methods that they subscribe as well as what they require from a reporting standpoint, but their backgrounds differ significantly. IFRS stem from the International Accounting Standards Board (IASB), which was preceded by the International Accounting Standards Committee (IASC). The IASC would draft International Accounting Standards (IAS), and today, rules made by the IASB are IFRS. The IASC was birthed by a group of countries to create a framework of uniform accounting standards (Financial Accounting Standards Board, Comparability in International Accounting Standards). Throughout the years, many countries have started using IFRS as a guide for all things accounting, though each country differs at least slightly in the degree to which it adopts IFRS. The history of U.S. accounting standards on the other hand has been centrally based on providing the United States with accounting standards for its own companies and companies that operate in the country. Many different accounting bodies have been in place at different times throughout the twentieth century in the U.S. The differing backgrounds of GAAP and IFRS continue to show this trend of differences between the frameworks, not only from a micro-level perspective with minor rule differences, but also from the standpoint of background and history.

With different backgrounds, it is safe to assume that GAAP and IFRS are put out by different organizations. As mentioned, the IASB drafts IFRS, while the Financial Accounting Standards Board in the United States drafts GAAP. One particularly consequential phenomenon is the fact that neither organization has real end-all authority. They are simply rule-making bodies. What sets the FASB apart, however, is the Securities and Exchange Commission. The SEC holds the authority to set and ultimately regulate accounting standards in the U.S. and any company that must file documents with the SEC. The SEC simply delegates to FASB the task of making and overseeing accounting standards. The purple elephant in the room for proponents of IFRS is the fact that the IASB has no repercussive authority to enforce. This is the resounding theme that rings out about anything related to international organizations that incorporate rules for several different countries across the world.

The IFRS mission is wrapped up in the idea of creating standards with useful qualitative characteristics that can be used worldwide by many different countries and world economies:

> Our mission is to develop IFRS Standards that bring transparency, accountability and efficiency to financial markets around the world. Our work serves the public interest by fostering trust, growth and long-term financial stability in the global economy. (IFRS Foundation,)

According to the FASB mission statement:

> The collective mission of the FASB, the Governmental Accounting Standards Board (GASB) and the FAF is to establish and improve financial accounting and reporting standards to provide useful information to investors and other users of financial reports and educate stakeholders on how to most effectively understand and implement those standards. (Financial Accounting Standards Board, “About the FASB,”, FASB Mission section, para. 1)

It can be noted that both FASB and IFRS are in the business of developing effective accounting standards. IFRS however, references “financial markets around the world” and “the global economy” (IFRS Foundation, para. 1). It is obvious that IFRS has a focus of becoming the primary framework for accounting standards, not just for countries currently implementing it but all countries in the world, and all world economies. The IFRS' reference to the "global economy" only serves to show that the focus of international standards is to benefit the entire world through its implementation on a global scale.

FASB, which puts out GAAP, on the other hand, makes no reference whatsoever to the world. It explains an aim to facilitate excellent accounting standards for the benefit of users. FASB is a U.S. organization for U.S. companies, and its mission statement doesn't mention about any kind of global economy, or overreach into other nations (FASB Mission section). The differing focuses and agendas of GAAP and IFRS are well exampled in the mission statements presented by FASB and IFRS. The merging of organizations requires the cooperation and merging of both organizations' missions. While the missions both point towards providing stellar accounting standards, they have different aims in terms of what vicinity they aim to serve.

As facts about GAAP and IFRS are discussed, and differences are uncovered, questions arise. Questions regarding when, why, how, and where are all viable when considering this idea of convergence. It is imperative to painstakingly undergo thorough due diligence in analyzing potential facts and consequences of IFRS and GAAP converging. While these questions and many others are important and interesting to find answers to, perhaps the most pressing question has to do with whether or not the convergence process should move forward. Convergence was a hot topic throughout the first decade of the twenty-first century but since then, the process has stalled and progress seems to have come to a grinding halt. Perhaps other political issues took the forefront as a new president stepped into office amid what is now known as The Great Recession.

The question of "whether" is what adds relevance to the sea of information about accounting rules. Convergence is a real-world issue with considerable effects on entire economies, and the world economy at large. Consequently, answering the question of whether convergence should take place opens the possibilities of unprecedented repercussions. As with many sets of choices, it can be easily assumed that many pros and cons accompany either alternative.

Many facets of society, from a macro to a micro level could be affected by convergence taking place. Based on the common differences that exist between GAAP and IFRS, it is clear to see that, should convergence take place fully, substantial change would occur. Even to move to the next levels of progress in convergence, changes would be needed that integrate the rules. GAAP allows and prohibits various accounting methods that IFRS might have the opposite stance on, and vice versa. Every detail would need to be agreed upon as to what would work best for not just the world, but the United States specifically, given its far-reaching, powerful, and impactful economy.

As detailed in the review of the literature, one of these areas of change would be tax. Accounting firms would have to understand the new rules as they relate to how to prepare taxes given the revised book accounting methods. Not only would professionals familiar with GAAP have to assimilate to the converged principles, but from a tax standpoint, these professionals might have to jump through an entirely new set of hoops to convert converged book numbers to taxable income via new book/tax differences, thus changing the world of public accounting on the tax side. The IRS also might have to accommodate the new rules by guiding tax filing business that use whatever new standards would come about because of convergence.

Another area that would be heavily affected is private accounting. Accounting services for small, medium, and large companies would be tailored to fit the set of converged standards derived from such a phenomenon. These standards would have to abide within the new framework, whatever it may look like. Perhaps the SEC would start requiring companies to file financials based off of the revised, converged standards. Implementing this change would take mass amounts of training, time, and resources.

Another way convergence would affect society would be in how it changes financial information. Company stakeholders often utilize financial information from companies in order to make decisions. Convergence would create one new set of amended accounting rules, from which could spring a change in numbers, measurements, and formats of financial reports because of the change in methods used to attain the given numbers. Consider LIFO, for example, which isn’t allowed under IFRS. Should the frameworks converge, the new set of standards would either keep prohibiting LIFO as an inventory reporting method, or allow it. If LIFO would be prohibited, many large companies that use LIFO would have to go through a comprehensive process to switch to an alternative method such as FIFO or weighted average, thus changing the bottom line. Should LIFO become perfectly legal everywhere as an inventory method for reporting purposes, then many companies that were under IFRS before may consider switching to it. This would end up necessitating greater awareness from all users of financial information, as the new set of rules would likely change what’s allowed for either the countries that currently use IFRS or the ones that currently abide by GAAP. Investors, consumers, professionals and anyone interested in company financials would have to understand what different elements would be in play with a new set of accounting standards.

People can decide for themselves on each little issue relating to whether one particular GAAP directive is better or more appropriate than an international standard. The problem becomes then that each GAAP rule that differs from its IFRS counterpart must be dissected. After everything is thought through, some U.S. rules might seem superior, while others subpar to IFRS. This phenomenon adds complexity to any sort of progress toward moving the convergence process forward. Then there is the step of looking at ways to reconcile the standards so that one converged upon set of guidelines can be formed. This would not only be a lengthy and expensive process, but would include multiple people, personalities, organizations, and so forth, all of which would have differing views on what is best.

Two other alternatives to this chaotic hyper-detailed approach seem quite viable in the process of answering the question of whether convergence should take place. One would be to simply accept things how they are. GAAP and IFRS are separate accounting guideline systems, that govern different countries. This alternative can be looked at as the way of, perhaps ease, but also ignorance. With so much thought about converging, along with some progress over the years towards it, work would have been wasted to just turn around now and discontinue any effort to merge GAAP and IFRS.

Perhaps the best way to assess whether convergence should take place is to examine the big picture. This would involve taking note of the world at large: its economies, its businesses, its people. This assessment would give equal thought to converging the frameworks and also keeping GAAP and IFRS separate and leaving things as they are. It would look at the big-picture advantages of converging versus not, and help reveal potential long term effects the world might end up with, should the process move forward. Not only would more objective measures play into this arguing, but also the more subjective, broader-scoped realities of politics and world views.

What is the biggest, most attractive element of possibly converging standards? Logically speaking, and what people have argued throughout the process, is that the big advantage rests in the idea of increased comparability. Essentially, this means that financial statements for many more companies in many more countries are much more easily comparable to U.S. companies that originally used GAAP. Suddenly, a company in the European Union and a company based in the U.S. in the same industry produce financial statements and the user can put them side by side and more quickly draw comparisons and conclusions about the companies' finances.

Another big advantage of converging the standards could be greater efficiency. Investors wouldn't have to decipher between what's prepared using GAAP and what's prepared using IFRS to determine sought after financial information. The effect of this would likely be quicker decision making in internationally-affected decisions. Convergence would lead to consolidation. FASB and the IASB would be able to work together and pool assets, expertise, and human resources to form a joint team to oversee and set standards. More countries would likely follow the U.S in moving towards international principles by adopting IFRS, leading to even more cohesion. Comparability, centralization, and efficiency seem to be just some of the possible benefits of a movement of GAAP towards convergence. The result would be a streamlined system, where accounting is dealt with in a consistent manner all around the world. With one worldwide set of accounting standards, it would likely become a much easier and faster process to determine the given rule for a phenomenon. This would stop researchers from having to first determine what guidelines are being followed since there would only be one framework. Furthermore, both for tax and reporting purposes, there would never be question as to what framework should be used since there would be one central go-to set of standards. In other words, having one big system would eliminate any confusion about what framework is used and what should be used.

To zoom out a little bit, it seems that these principles of increased comparability and efficiency by consolidation could apply to much more than just accounting standards. Take companies for example. Often mergers and acquisitions take place in order to synergize operations. The result can be minimized costs and increased profits. More centralized means more streamlined, and more streamlined can lead to more efficient, and therefore in the end, more lucrative.

The idea of mergers and acquisitions isn't merely confined to the world of business and accounting. This type of activity can occur in government and politics. Consider anything from the great conquests of old where empires were sweeping through and acquiring territories or the great land acquisitions that occurred in the early history of the U.S. Many other examples of acquisitions chronicle the history of countries growing and control being taken over a larger land mass.

Perhaps a modern example of a trend towards this merging of entities is Europe. From the 1950's up through the 1990's, a steady progression towards European integration was in the works. In 1993, it was finalized by the Maastricht Treaty and the European Union was formed ("A Timeline of the EU," 2007, 1993 section). Today, 28 countries are members of the EU. These countries are allies that share a set of security and economic standards. In 2002 the Euro was put into play as a common currency for countries in the EU ("A Timeline of the EU," 2007, 2002 section). The forming of the European Union and the adoption of the Euro as common currency were big steps in the process of converging the politics and economics of many countries across Europe. With the European Union in place, certain efficiencies and privileges were afforded each country that was a part of it. For example, borders between EU countries were open, meaning people could easily go from one country to another. Trade and transportation also were eased through such an integration of countries. The formation of the EU also naturally put in place a strong core of allies that are dedicated to defending each other militarily. One detail to note, however, is that with the EU's formation came the necessity of some sort of centralized power. Representatives of select nations rotate each year in leading and overseeing the EU.

This centralized power in the EU is case and point to the reality that naturally presents itself in the event of any merging of systems. When companies merge, all of a sudden, a leadership group is in place that oversees more people and territory than any single leadership group before such a merging. This centralization of power theoretically presents some potentially positive elements. One such attribute of centralized power is the ability to make decisions quickly. This goes hand-in-hand with another possible advantage which is more cohesion and efficiency in the decision-making process in general.

This cohesion must be present in some way no matter what system is in place, not just in a company, but also in countries. The U.S. for example is a country known for being rooted politically in the idea of checks and balances in government. A bicameral congress makes and passes laws in the process known as legislation. The president is a check on congress, given that he has the authority to sign into law or veto the legislation passed by congress. But the legislative branch is conversely a check to the executive branch, the president. This is evidenced in the capability of the senate to impeach the president, and other various practices the senate goes through, such as holding hearings to approve a president's chosen cabinet members. The Supreme Court can make decisions that declare whether certain laws, practices, or executive orders are constitutional or not. The president appoints each member of the Supreme Court, each of which are allowed to serve life terms. Each body is different in nature. In contract to Supreme Court justices, presidents and congressmen serve within limited terms. Perhaps one example of centralization of power in the U.S. is the president's status as commander and chief. This means the president oversees the military and can direct military operations and the deployment of weapons for both defensive and offensive purposes at any given time. While the U.S. is known for having balances of power, the power of the president to direct the military is an example of centralized power. And the justification of this consolidation of power over the military is that the military will be able to move quickly due to greater decisiveness from the top.

This same quality of easy and quick decision making that accompanies more centralized power isn't without its drawbacks. While quick decisions can increase efficiency, move processes along faster, and fix problems in a timely fashion, they can sometimes have hidden and unexpected consequences. For decisions to be helpful to a society, two elements must be in place. First, the people making the decisions must have inherently good motivations for the welfare of others. And secondly, there must be at least some form of objective support and evidence that points towards the decision having positive consequences. In other words, expertise and information play a key role as well as good intentions. If the people in power have good intentions and expertise or expert counsel advising them to make those decisions, then the result will be decisions that benefit and serve people and carry out justice. However, corrupt centralized leadership could wreak havoc, making decisions that could benefit themselves or their families at the expense of others. Or good but simply ill-informed, incompetent leadership could make decisions that turn out to have gloomy consequences.

A second attribute of centralized power that could be both a blessing and a curse relates to efficiency with resources, human and financial. The fewer the people in power over a jurisdiction, the less costly it is to operate the government from a human resources standpoint. This would free up more wealth to be used for necessary programs and other vital dealings. Furthermore, with less people in power, more people are freed up to participate in the private sector, which in turn generates more activity in the economy. On the other hand, efficiency might be lacking in the sense that less checks and balances and more centralized power could result in less well-rounded thinking. For example, one person with the capacity to lead and authority to make decisions might cost a government less in terms of compensation. However, two people, or better yet, an advisory committee might generate far more expertise in various aspects of the government that add value to decisions, and outweigh the benefit of simple having less compensation expenditures.

These examples of pros and cons to power centralization in entities or countries can serve as examples to how centralized power might impact the world of accounting standards. As it is, IFRS and GAAP are separate frameworks overseen by two different boards. In the U.S., the SEC has the ultimate authority over accounting standards, but has delegated the responsibility of making them to FASB. IFRS is the system put into place by the IASB. As it is, it is these two bodies that run these two separate frameworks. IFRS and GAAP dictate what almost all the major countries in the world use as accounting standards. With two systems in place, research can always be done as to what the differences between the frameworks are. Researchers can compile data and perform studies compare the effectiveness and strengths of the frameworks. GAAP rules could perhaps look to IFRS and take note of some rules that might be great to add. And international standards could potentially also benefit from examining GAAP and using the findings to improve as well. In other words, the two frameworks can constantly be improving to form the best rules for each given topic in accounting. In a sense, this reality of constant improvement and competition between the standards could conceivably be thought of as a very gradual and organic converging of principles. The reason for this theoretical convergence would be that if both frameworks are constantly improving and aware of each other, they could naturally drift towards similar rules for given topics.

With this mindset regarding competition between the two standards' frameworks, it's clear to see that one could make a case study of one topic and examine the results of a GAAP rule against an IFRS one. Having the two standards provides almost a test lab environment where researchers and accounting professionals can see how certain rules affect accounting and what principles really work in promoting ethics and keeping companies accountable. All in all, having two sets of standards could be a very helpful reality conducive to learning and measuring the effects of some rules over others. The data is turned into information, the information then can be used to update rules when needed and facilitate moves towards superior standards.

Imagine the world having only one instead of two prevalent sets of accounting standards. This competition that exists between GAAP and IFRS would be non-existent. Progress towards improvement in accounting standards would be at least twice as slow. The reason for this is that with only one main system in place there would essentially be nothing else to base it off of and learn from. There would be no other widely used framework from which to glean from in terms of best practices as well as what doesn't work. This is all assuming that there would even exist motivation to constantly improve the standards in the first place. With one set of standards, while things might slowly improve, there might be a lack of forward thinking that currently exist with GAAP and IFRS operating separately. Having only one system would quickly turn accounting standards into a monopolistic phenomenon. One organization would control accounting standards for most of the world. No matter how effective or ineffective the rules would be, there wouldn't exist the same accountability that comes with having other frameworks to compare to and evaluate.

When organizations, functions, and rules are converged and consolidated, a key question emerges about validity – validity in the form of whether actual authority exists. Organizations can pose as having authority, but if there are no grounds or basis to enforce whatever rules spring up, then the authority is artificial. This is true of international ventures such as the failed League of Nations that preceded the United Nations, which is in place today. International ventures generally are started out of certain common interests between different countries. The result is organizations that don't possess real authority but serve as affiliative agents and facilitate special alliances, relationships, and pooling of ideas between countries. Given that IFRS isn't controlled by one country, there is no mode of discipline or enforcement of regulation for countries that use it. Perhaps this is why over 100 nations are said to implement IFRS as the basis for accounting standards.

Proponents of the convergence might attempt to convey IFRS in a strong, bindingly authoritative light. It really represents simply a common thread of ideology relating to accounting standards – common accounting guidelines, through which basic themes are instrumental in providing a basis for the financial standards of many nations.

CONCLUSION

Different nations have different characteristics. It may be relatively easy for small countries to adopt IFRS as a preferred accounting framework. It may even be quite helpful and beneficial to developing countries to have a ready accounting system to adopt. The U.S. and China, however, are examples of large, powerful nations that utilize standards frameworks separate from IFRS. The U.S. and China both have their own very large, complex, and influential economies, that affect much of the world. With GAAP as the basis for accounting in the U.S., it is only conceivable that rules are instituted that facilitate accounting in a way that is distinctly helpful for the United States and professionals that work for U.S. companies.

Furthermore, U.S. standards are authoritatively binding on U.S. companies that must file with the SEC. This means that actual laws with consequences dictate and facilitate the regulation of accounting standards in the U.S., thus legitimizing the necessity to follow the rules. If IFRS and GAAP were to converge, questions would be sure to arise regarding where authority would stem from in such a system. The U.S. is a powerful nation that historically is willing to sometimes to make trade deals and affiliate with other countries in alliances, through representation and participation in the U.N. However, the Constitution is the supreme authority in the U.S. No international body can restrain and impose laws on the United States.

Given this authority phenomenon, where would the authority to set international uniform accounting standards stem from? What mechanisms for enforcement would be put in place to ensure that theory translates into practice? Perhaps these difficulties have helped stall the convergence process between GAAP and IFRS. Would authority be put in the hands of an international body? If so, would this centralized power be paramount to a governing body with authority over independent nations such as the U.S. that would ascribe to the international accounting standards?

Two pictures of a converged international system seem possible. One of these pictures is of a system where no real authority exists. This would be the case because each country has its own sovereign authority to govern itself. IFRS and GAAP could both compromise, but the U.S. would end up adopting the international uniform standards and enforcing them within the country. Each other country would have to take on some of the changes that IFRS had to accept to converge with GAAP and the U.S. would likely have to adjust to the new hybrid.

The second picture is one where authority is granted to an international body, possibly the UN or the IASB to oversee and regulate the practice of the converged set of accounting standards. For real authority to exist, however, ability to enforce the rules must accompany the regulation itself. For this to be the case, nations that adopt the international standards would be opting in to be regulated by an international body. The U.S. would be putting itself under the authority of an international body that would have the authority to penalize companies and practitioners that fail to keep proper standards, in essence, compromising the very sovereignty that defines the nation's independence.

Part of the mess that would ensue given convergence into one world accounting system would be the political state of affairs. An internationally comprised body would be able to dictate standards that hold precedence within individual, sovereign countries, including the U.S. It is unclear what stance the SEC would take regarding how much power to give over to whatever joint accounting system would be in place. However, the idea of consolidating IFRS and GAAP has consequences that are at the very least, difficult politically.

As exampled earlier, the European Union is a prime example in a globalist movement by nations in the twentieth and twenty first century. Actions by the U.S. government to reach out and form alliances with other countries, militarily and economically, further substantiate the notion of increasing globalism. One historic event of note was the 2008 election. On the domestic side of things, the people of the United States were ready for change from how things were, with a failing economy and being in the middle of what was known as the Great Recession. On the international front, however, an agenda of reaching out and being quite involved with international endeavors was prevalent with the incoming Obama presidency. Convergence itself didn't move forward during the Obama years but this was by no means an indicator of less world involvement from the U.S.

This post-world war movement of converging and forming various economic and political alliances can be seen as progress towards globalism. Examples of globalist efforts throughout the twentieth and early twenty-first centuries are numerous such as anything from the EU to the UN. Peace through unity has been the resounding theme of these attempts to centralize power.

These moves towards globalism haven't been met without resistance. A surge of nationalism erupted near the end of the Obama era. Simply put, people in the U.S. became disenfranchised with foreign policies giving exorbitant aid to unstable foreign nations, trade deals that didn't afford the U.S. maximum benefit, and policies that drove manufacturing and related jobs out of the country. While a heated presidential election was taking place, other countries were getting restless with the globalist direction the world had been going. This birthed the Brexit movement, in which the people and parliament of Great Britain voted and opted to secede from the European Union in the summer of 2016. Later in the year, the historic election of Donald Trump came to fruition in the United States. Trump touted his experience in business and proven negotiation skills which could be used to "Make America Great Again."

Theresa May, the prime minister of Great Britain was, incidentally, the first foreign leader to be in a joint press conference with the new President Trump ("Trump Has First News Conference with a Foreign Leader," 2017). In some ways, the moves toward nationalism in the U.S. and Great Britain ignited and revived tremendous mutual respect, that in some ways united the two in the common bond of being nations that looked out for the interests of their own people first, rather than striving for international unity. In other words, nationalism bore a natural and mutual unity between the two countries.

This recent swing in politics has moved the convergence process from being dormant, to virtually the point where it's hardly mentioned in the business world. Maybe this is due to so much other relevant activity of late. Or maybe this is because convergence poses two frighteningly consequential possible outcomes.

With the first picture mentioned where the organization in charge of the converged standards has no real authority, a U.N.-like institution would be the reality. Accounting standards will be simply recommended, and the idea of countries following international principles would be closer to a loose group of affiliated countries that have open dialogue about accounting standards. The biggest change that would take place on a regular basis would be that money has to be poured in to keep up this international standards framework, that has no real authority.

With the second picture talked about, the U.S. would be subjecting itself to the authority of an international body. Having a strong, centralized system would likely result in financial information being streamlined. Financial statements across the world would have similar formats, and the enhanced comparability would make many elements of the world economy far more efficient.

The centralized system would afford many benefits to the world economy in terms of unification. But as is always the case, increased risk would accompany the increased reward of one world financial accounting framework. Having one comprehensive set of principles that applies to the world would likely lead to other steps to unify the world economy. Perhaps a global financial market would be created that merges prominent stock exchanges into one global conglomerate. With the boom in the one-world economy movement, regulation might be necessary. For regulation to be effective, enforcement from a top level would have to take place. In effect, the world would have to be governed, thus centralizing power over not just individual nations but over the entire world.

The question remains… should this happen? As in much of the world of economics the answer depends on what people demand. What do people want – the system to remain as is, or a system of enhanced comparability, with the cost of the United States virtually losing its independence?

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Appendix

Income Statements Table for Bratton & Cunningham (2009)'s Review

Classification of "extraordinary items"	*Allowed*	*Prohibited* (unusual items can be segregated)
Restructuring costs	Recognized when little discretion to avoid costs exists (mostly when incurred)	Recognized or announced when commenced

Intangible Long-Lived Assets Table for Bratton & Cunningham (2009)'s Review

Research Development Costs	*Expensed* as incurred; included in *operating* cash flows	Research costs expensed as incurred; development costs *capitalized and amortized*; portion capitalized included in *investing* cash flows
Estimated residual value	Present value of expected disposal proceeds	Current net selling price, assuming asset is in expected age/condition as at end of useful life
General Impairment Tests	Fair value	Higher of *use value or fair value less costs to sell*
Goodwill Impairment Test	Special test compares fair value of cash generating unit to book value, then compares good-will to carrying value	No special test (use one similar to other long-lived assets, a single-step computation
Impairment Reversals	*Prohibited*	*Permitted* in some cases
Revaluations	*Prohibited*	*Permitted* in some cases

Revenue Recognition Table for Bratton & Cunningham (2009)'s Review

Service Contracts	Generally, amortize over service period without up-front recognition	Allows up-front recognition when partial performance has occurred
Multi-Element Contracts	Defer recognition on delivered portion if non-delivery of remainder triggers a refund	Recognize on delivery of portion even if non-delivery of remainder triggers a refund, so long as delivery probable
Long-Term Construction Contracts	Allows percentage of completion method to be approached using either revenue-cost or gross-profit measures *Requires* completed contract method in certain circumstances	Requires revenue-cost approach to percentage of completion method (unless percentage not reliably estimable, in which case requires cost recovery method) *Prohibits* completed contract method