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## Lobbying in Accounting Standards Setting

By Afzal Ahmad

*International Islamic University Chittagong, Bangladesh*

**Abstract-** The paper explores the effects of lobbying on accounting standards. The study investigates the determinants of lobbying and compares the lobbying activity with application to the FASB Statement of Financial Accounting Standards No. 158 and the IASB Statement of Intent issued in 1990. The research concludes that the major determinants of lobbying in the field of accounting standards are the size of lobbying corporations and the perceived effects of the regulations on the economic well-being of the enterprises. The analysis of the specific cases indicates that both firm-level, industry-level and country-level factors contribute to lobbying decisions across firms.

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# Lobbying in Accounting Standards Setting

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## I. INTRODUCTION

Standard-setters, including the International Accounting Standards Board (IASB), formerly the International Accounting Standards Committee (IASC) and the US Financial Accounting Standards Board (FASB), are committed to protect the interests of investors rather than the interests of corporations and auditors. However, political lobbying can take place due to the self-interest of preparers or governments. Thereby, standard-setters may have incentives to modify their positions and dilute or abandon the principles of the standards (Nobes and Parker, 2008). At the same time, lobbying on behalf of corporations may take place, as suggested by different theories (Nobes and Parker, 2008). Nevertheless, the factors that contribute to lobbying are not univocally identified in literature (Georgiou and Roberts, 2004; Koh, 2011).

The aim of the current paper is to explore the possible determinants of lobbying and its effects on standard setting in accounting. The objectives of the study are to compare the lobbying cases against the IASB and FASB statements and to identify what factors drove the decisions of different parties to lobby in these cases. The paper includes the literature review and the analysis of the lobbying activities with reference to both IASB and FASB cases. Besides, the study explores particular statements of the FASB and IASB and analyses how the specifics of these statements determined the decisions of different parties to lobby for or against the proposed acts.

## II. LITERATURE REVIEW

Accounting lobbying can be explained by a number of economic and managerial theories, including the agency theory and stakeholder theory (Hoffman and Zulch, 2014). The agency theory suggests that

regulatory agencies that introduce standards include those who are regulated. This implies a conflict of interests between the parties (Mathur et al., 2013). In contrast, the public interest model argues that regulators represent the interests of the society, while the conflict of interest still may take place in the relationships between the regulators and the public (Hoskisson et al., 2011). The stakeholder approach takes into consideration the environment of the firm, including customers, suppliers, and employees. These parties are the stakeholders of the enterprise and lobbying decisions of these parties are determined by the stakeholders who possess power, urgency and legitimacy (Freeman et al., 2010).

The harmonisation efforts of accounting standards that had been undertaken by the IASC faced different barriers, including cultural, economic, political and other factors (Garrido et al., 2002). In the meanwhile, Larson and Brown (2001) explored the relationships between the harmonisation efforts and accounting standards lobbying. Particularly, the study analysed the effects of the countries' financial accounting standards and the countries' tax rules on lobbyists' position. The research focused on long-term construction contacts and confirmed that lobbying position was associated with the mentioned variables. Every factor could prevent the harmonisation process. However, the research by Koh (2011) analysed the drivers of companies' decisions to lobby and found the factors that contributed to lobbying. The factors included to managers' option compensation and companies' closeness to debt constraints. Besides, smaller companies in a sector with peers who had lobbied, the firms that had board relationships with such firms, and the enterprises that had higher degree of board independence were more likely to lobby.

The research by Georgiou and Roberts (2004) also explored the determinants of lobbying through a logistic regression and concluded that size and previous lobbying experience were the most significant determinants of the decisions to lobby. Furthermore, the firms that lobbied against the proposals had debt covenants in contrast to the companies that lobbied in favour of the proposals. Nevertheless, debt covenants were not able to explain the differences between non-lobbying behaviour and lobbying against. Incentive compensation effects were inherent to the companies that lobbied in favour. It is suggested that the decision to lobby is determined by the economic effects of a particular rule for the company (Deakin, 1989). However, these effects imply managerial perceptions rather than

actual outcomes. The analysis of the lobbying program by oil and gas enterprises demonstrated that the decision to lobby was associated with the possible effects of accounting methods on the economic well-being of the company and its managers.

The observations about the significance of the effects of regulations on the economic well-being of the firm for lobbying decisions were obtained by the research of Hill et al. (2013). However, the authors performed a cross-industry analysis and found that the variation in lobbying activity across different sectors was large. In addition, companies used multiple channels of possible political influence to affect regulatory and policy outcomes. The potential payoffs from favourable policy and regulations were found to be the most significant determinants of lobbying. At the same time, the research showed that managerial-shareholder agency problems were not associated with the lobbying activities of the politically active enterprise. Some studies explored the lobbying practices under different regulatory regimes, such as the FASB and the IASB (Hodler et al., 2013; Dye and Sunder, 2001). The research by Johnston and Jones (2006) explored not only lobbying in different industries, but also lobbying practices under different accounting standards, including the FASB and the SEC (u meant that FASB and SEC also work as a lobbyist). The authors showed that companies' lobbying expenditures were related to the incentives to lobby on the problems associated with accounting. Specifically, lobbying expenditures were positively related to a company's exposure to amendments in the accounting standards. Nevertheless, this relationship was captured only to occasional lobbyists. Furthermore, the firms that did not have a lobbying department and made income-increasing accounting choices were characterised by higher expenditures on lobbying.

### III. IASB AND FASB LOBBYING

The analysis covers the investigation of lobbying cases on both IASB and FASB. The exploration of corporate lobbying under the accounting standards set by the IASB shows that company size is associated with lobbying. Empirical findings showed that large corporations were more likely to write comment letters to IASB, as these enterprises were a part of the Forbes Foreign 500, while 23 out of 27 US lobbying companies were comparably large (Larson, 1997). However, the findings also demonstrated that the rate of large enterprises' decisions to lobby was different across countries. The highest percentage of lobbying companies was observed in Australia, Hong Kong and Switzerland. By contrast, such countries as Italy, Spain and Korea had no companies that lobbied, despite having large enterprises listed on the Foreign 500 (Larson, 1997). However, there are some factors that may prevent lobbying, and these factors are not

associated with the consent of the IASB. An empirical analysis of UK investment management companies showed that the major factor that inhibited lobbying by the companies was the cost of lobbying. At the same time, the questionnaire survey demonstrated that the participation of the companies in lobbying activities was not low (Georgiou, 2010).

The analysis of the effects of political and lobbying forces on accounting standards in the US with application to the FASB demonstrated that there is no clear conclusion about the opportunities of such forces (Gipper et al., 2013). Particularly, while oil and gas accounting was substantially affected by lobbying in the 1970s, the importance of political forces in general was not captured by the analysis of different empirical studies of lobbying. Nevertheless, in line with lobbying in Europe, company size was positively associated with lobbying activities. This fact could be explained by larger potential costs in the regulatory processes for such enterprises. On the other hand, the size directly influenced a company's influence and the probability of success (Gipper et al., 2013). Nevertheless, the resistance to FASB accounting standards can be determined by different factors beyond the corporate level. Specifically, the empirical study concluded that lobbying determinants could be attributed to the standard, the corporation, and the industry levels (Elbannan and McKinley, 2006). The analysis of these three levels showed that lobbying was associated with the perceived uncertainty introduced by a FASB standard, the information-processing requirements of a standard, the requirements to deviate from institutionalised financial reporting practice, a company's ability to acquire scarce resources, the dependence of the corporation on external stakeholders and the power of the firm over stakeholders, thus confirming the stakeholder theory.

An analysis of the lobbying behaviour in response to a particular act showed the significance of company-level factors. The Statement of Financial Accounting Standards (SFAS) No. 158 was titled "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" and was introduced by the FASB in 2006 (Houmes et al., 2012). The exploration of the enterprises that lobbied in regards to this statement showed that the decision to lobby was associated with the underfunded plans of the companies and the possible effects of the SFAS No. 158 on the adjustments to the balance sheet. Thereby, the differences between recognition and disclosure from the managerial perspective were captured, as lobbying was related to the perception of managers of the relocation of disclosed information in the financial statements and the recognition of the information on the balance sheet (Fried, 2012).

An analysis of IASC/IASB statements also demonstrates the attempts of lobbying. For example,

the IASC Statement of Intent issued in 1990 suggested that last-in-first-out principle should not be applied by the companies. However, the principle could be used for income tax purposes in such countries as Italy, Germany, Japan, and South Korea, as the countries had intertwined tax and financial reporting (Whittington, 2007). The delegations from these countries voted against the elimination of the principle. This case confirmed the agency theory, as it demonstrated the presence of the conflict of interest. Besides, the case showed the significance of country-level factors that could determine lobbying decisions in the international settings (Nobes and Parker, 2008).

#### IV. CONCLUSION

The paper investigated the determinants of lobbying in the field of accounting standards setting and found that the factor that was most often mentioned in literature and observed in the case studies was the size of the lobbying company. Furthermore, the decision to lobby was determined by the possible effects of the act or statement on the financial performance of the enterprise, according to the perceptions of the managers of this firm. The comparison of the IASB and FASB acts showed that the determinants of lobbying could be related both to the company-specific and country-specific factors. In addition, the literature review indicated the importance of the industry level in terms of the propensity of companies to lobby and the effects of lobbying on standard setting in accounting. The research confirmed both the agency theory and the stakeholder theory. From the agency theory view, lobbying in accounting standards setting takes place when the conflict of interest between the society and the standard setters or companies is observed. From the stakeholder theory perspective, enterprises care about the most powerful and legitimate stakeholders when undertaking lobbying efforts.

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