

FRANCE AND INTERNATIONAL ACCOUNTING STANDARDS:

UNE BALLE DANS LE PIED?

(a self-inflicted wound?)

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Abstract

This paper explores the juxtaposition of IFRS and the PCG. We argue that the significant difficulties are logically inevitable and predictable, and were self-imposed by France through a mechanism of its own choosing. We outline philosophical arguments that reality (including economic reality) is a community-specific perception, and explore the twin realities of IFRS and the PCG, showing that differences are *a priori* both rational and significant. We provide detailed primary evidence via in-depth interviews to illustrate our general argument, and conclude showing that all the aspects of our coverage support and justify our title.

Keywords

IFRS. PCG. internal reality. provisions. contingencies.

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1. INTRODUCTION

This paper investigates recent developments relating to the spread of IFRS influence and ethos in and into the French context. The author team can be characterised as Anglo-French, in terms of nationality, language ability, and cultural awareness. This enables us to attempt to distance ourselves from both technical minutiae and political rhetoric. Our analysis is independent, but certainly not anodyne. In essence, we argue that the significant difficulties arising from the introduction of IFRS regulations into French *national* requirements (the plan comptable general, PCG) were logically inevitable, predictable, and self-imposed.

We outline some theoretical and philosophical underpinnings, in section 2, and then explore the distinctive realities of IFRS accounting in section 3 (briefly) and of French accounting in section 4 (in more detail). Section 5 provides important primary evidence of the problems of integrating IFRS-origin regulations into the French accounting psyche resulting from a series of in-depth semi-structured interviews relating to provisions, contingencies and IAS 37. Section 6 briefly concludes.

Note The extensive French language quotations are an important part of our evidence and argument. In this version of the paper they are given in full by way of appendix, and we give English versions in the text. These translations are at times close to indicate the style of presentation and thinking, and occasionally “free”, to indicate the sense. We do not claim a high level of literary artistry.

2. SOME THEORETICAL UNDERPINNINGS

We do not have the space, nor would it assist the specific focus of our paper, to develop detailed philosophical underpinnings. Suffice to say that we broadly accept the idea developed in a number of recent papers (e.g. Shapiro, 1997, 1998; Alexander & Archer, 2003; Mouck, 2004), not always quite consistently with each other, applying to the accounting domain the concept of institutional and inter-subjective reality developed by Searle (1995, 2006a, 2006b).

Many “objects” exist only through generally agreed social construction. Metal exists without human thought (equals social construction), money does not, being, by definition, a generally accepted median of exchange, between members of society who choose to accept the notion and operate within its applications.

Searle’s (1995) theoretic starts by making an ontological commitment to physical objects (brute facts), and then, based on the concept of “intentionality” explains how social objects come into being. According to Searle (1995) people have the *ability to share beliefs or desires* – termed “*collective intentionality*” – that in certain conditions can give rise to a specific type of social facts, namely, *institutional facts*. More exactly, *institutional facts* come into being by ascribing a *status function* to a physical object (*brute fact*) by means of *collective intentionality*. This is done by a performative utterance in the form of: “X counts as Y in the context C” (where X is the brute fact and Y is the institutional fact). For example: “Bills issued by the Bureau of Engraving and Printing (X) count as money (Y) in the United States (C)”.

This rationale is used in accounting to describe how accounting concepts are socially constructed

“By virtue of collective intentionality, ownership claims, income, and other conceptual objects of accounting can, under appropriate conditions, be *institutional facts*.” (Alexander and Archer, 2003).

This paper is written in the context, and needs to be read in the context, of the principles of Saussurean linguistics. In essence this leads to three propositions.

- The use of a particular word as signifier (fr. signifié) is arbitrary. There is no rationale for, or significance from, cat being cat and not rumpelstiltskin.

- The use of a particularly conceived concept as signified (fr. signifiant) is arbitrary. The famous example, from Saussure himself, is that French conceives of two types of river, one that flows directly into the sea and one which does not. Two concepts require two words (un fleuve and une rivière respectively). English thinking never made this conceptual distinction, and therefore only has one word for the one concept: river.
- The relationship between a word and a concept is itself arbitrary. Cat could just as well signify a small nocturnal flying mammal instead of a furry four-legged, one tailed, friendly, independent and potentially vicious mammal, and bat the reverse.

All three “arbitrarinesses” are created and understood by collective acceptance, not by intrinsic rationale or fact.

Searle (1995: Ch 3, 2006b: 19) argues for an unavoidable relationship between institutional facts through collective representation and language. Over and above the intuitively obvious similarities regarding shared beliefs (institutional facts) and shared meanings (language) is the more fundamental point that the move from object (e.g. metal) to status function by means of collective representation (e.g. money) is only possible if there is a mechanism for creating, and communicating, this collective representation. “The essential thing about human beings is that language gives them the capacity to *represent*” (2006b: 19, emphasis original). We are now in a position to consider the intertranslation issue raised by McKernan (2007: 164).

McKernan (2007: 164) quotes Davidson (1974: 189), apparently favourably, as arguing that intertranslatability¹ has to be possible as “we cannot make good sense” of the alternative, because the alternative implies the existence of “different conceptual schemes or conceptual relativism”.

The logical link is immediately accepted. Languages are conceptual schemes, as the arguments from Saussure and Searle in the immediately preceding paragraphs show. Conceptual schemes are collectively accepted across a community. Different conceptual schemes would suggest different communities, and therefore a lack of intertranslatability.

One issue concerns the argument that if a clear logical reconciliation is possible, however long and convoluted, then there is no lack of intertranslatability. Arguably the issue of intertranslatability can be solved by means of equivalent expressions: un fleuve = a river flowing into the sea; une rivière = a river flowing into another river. But on the other hand the

¹ The word is surely tautological. Inter means between (two things) and trans means across (between two things). We continue to use it for consistency.

fact still remains that the two languages are constructed with two different conceptual frameworks regarding large volumes of water flowing downhill.

As a more detailed example, we instance a problem between French and German, not involving the English language at all. The extract below is from the advice of the “*avocat général*” presented to the European Court of Justice on 26 November 1998 in relation to case number C-275/97, as a ‘preliminary opinion’. The opinion relates to a case of German origin, was prepared in French, and exists also in official German (and Spanish, apparently) translations but not in English. Paragraph 11, reproduced absolutely verbatim, reads as follows.

La quatrième directive a été transposée en droit allemand par le Bilanzrichtliniengesetz (loi sur le plan comptable général) du 19 décembre 1985. Cette loi a été incorporée dans le troisième livre (articles 238 à 342) du Handelsgesetzbuch (code de commerce, ci-après le <<HGB>>) du 10 mai 1897.

The author has seen fit to explain Bilanzrichtliniengesetz, in French, as *loi sur le plan comptable général*. This is absolute nonsense. A literal translation of Bilanzrichtliniengesetz would be accounting guidelines law. But Richtlinie is the formal translation of directive (as in fourth Directive), so a proper translation would be “accounting directives law”.² But what has this to do with the *plan comptable général*? The answer is: absolutely nothing. Germany has no *plan comptable*, which is an internally specific French concept with a unique and context-specific ethos. It represents a conceptual scheme automatically understood in the French context, but alien, foreign, and incomprehensible in the German situation, which is the context about which communication is intended.³ The two conceptual schemes here are fundamentally different, and have been found to be not “intertranslatable”.

Our conclusion on the intertranslatability question is clearcut. This is that intertranslatability cannot be assumed. This is not just true in itself as a language issue, despite the significant implications (problems?) for conceptual relativism and the existence of different conceptual schemes. It is true *because of* conceptual relativism and the existence of different schemes.

Some of the ideas in this brief exposition are further developed in Alexander and Archer (2003) and Alexander and Ionascu (2008). The general implication of our argument is that concepts and notions are unlikely to be perfectly communicated across languages, and are unlikely to be understood and rendered operable in the second community in the same way

² This is supported in that the first draft of this law was anticipated to transpose the fourth Directive only, and was labelled Bilanzrichtliniengesetz (i.e. single directive). The eventual law incorporated three directives at once, hence the plural (*linien*, not *linie* in the middle of the composite word).

³ This is true, notwithstanding the fact that the *plan comptable* system was refined by Reichsmarschall Goering, and introduced into France at the point of a gun in 1940. This of course demonstrates its logical independence from European Union Directives.

as they were in the first community, even if they could be perfectly communicated in a language sense.

Before our analysis of the French “community”, in section 4, we present an outline of IASB thinking in the next section.

3. THE INTERNAL REALITY OF IFRS

The International Accounting Standards Committee, as it then was, was formed in London in 1973. This was the same year that the United Kingdom joined the European Community and the conjunction of dates is unlikely to be a coincidence (Hopwood,1994:243). The original members were the accountancy bodies of nine countries: Australia, Canada, France, Germany, Japan, Mexico, Netherlands, the UK (with Ireland) and the US. The original six members of the European Community were France, Germany Luxembourg, Belgium, Austria and Italy. Given the well-known fundamental and deep-seated historical differences between the Roman Law tradition and the relatively low importance of the external investor of the Continental European tradition on the one hand, and the Common Law tradition and the relatively high importance of the external investor in the UK (and all its former colonies, including the USA) on the other, the motivation of the UK in being keen to take a lead in the creation of such a body is not surprising. It was widely believed that at the EC (EU) level the UK would always be in a philosophical and political minority, whereas, given the membership and relative economic and political strengths of the original membership of the IASC, its position in the IASC would be very much stronger. History has amply justified both beliefs.

The IASC’s major problem was that, as a private self-created club, it had no real authority, and certainly no legal or regulatory authority, of any kind. It had no authority to force any of its members to accept standards which they did not like, and it had no authority to enforce the application of its standards. It could safely be ignored. It is only the agreement with IOSCO of 1995, and the active support of the European Union (which hated the idea of a world domination by the US FASB, which it could not influence, even more than it disliked the idea of world domination by the IASC, which it could at least try to influence), from the same year, that opened the gates to the important position which the IASB has today.

The Preface to IFRSs, taken from the IFRS Bound Volume current at 1 January 2007, states that the objectives of the IASB are as follows:

- (a) to develop, in the public interest, a single set of high quality, understandable, and enforceable global accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the various capital markets of the world and other users of the information to take economic decisions;
- (b) to promote the use and vigorous application of those standards; and
- (c) to work actively with national standard-setters to bring about convergence of national accounting standards and IFRSs to high quality solutions.

This makes it absolutely clear that the essential focus of IFRSs is on the provision of information for capital markets. It is apparent that this is consistent with the historical UK tradition, rather than with the historical European tradition.

There is a view, apparently widely held in certain countries, that there is an Anglo-Saxon, or Anglo-American, conspiracy at work, which has attempted, successfully, to impose its hegemony on the IASB, to achieve the objectives outlined above. See Flower (1997) for an archetypal example. This view is misleading, for two reasons. The first reason is that the concept of 'Anglo-Saxon' accounting is itself dangerous, or at best simplistic, in the 21st century. See the discussion in Alexander and Archer (2000, 2003) and Nobes (2003) and also Bush (2005). In the battle (the word is not overstated) between the Europeans and the Americans for the heart and soul of the IASB, for example over the principles versus rules dichotomy, (see Alexander and Jermakowitz, 2006), the UK is very much in the European camp. But the second reason is more positive. This is that the so-called Anglo-Saxon tradition of flexibility and relevance to the individual situation was designed, as discussed above, to provide investor-focused information. The objective of the IASB, already quoted, is to provide investor-focussed ('capital market') information. It is hardly surprising therefore that the philosophy of the IASB standards is broadly similar to the traditional UK-type philosophy. It is also hardly surprising that the IASB philosophy is very different from the traditional continental European (e.g. French) philosophy. The different internal realities relate to the different community contexts and purposes.

The IASB's approach to international accounting harmonization is currently built around IAS 1 which requires a fair presentation, rightly undefined. What we are told is that a fair presentation requires (para. 15):

1. Selecting and applying accounting policies as described in IAS 8.

2. Presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable, and understandable information.
3. Providing additional disclosures when the requirements in International Accounting Standards are insufficient to enable users to understand the impact of particular transactions or events on the entity's financial position and financial performance.

Judgement and subjectivity abounds in every phrase of the above. The crucial issue of selecting accounting policies is addressed in IAS 8. Most of what IAS 8 says in this respect is both sensible and rather obvious. When a standard or an interpretation specifically applies to a situation, the accounting policy or policies applied are to be determined by applying the standard or interpretation and considering any relevant Implementation Guidance issued by the IASB for the standard or interpretation. IFRS set out accounting policies that the IASB has concluded result in financial statements containing relevant and reliable information about the transactions, other events, and conditions to which they apply. Those policies need not be applied when the effect of applying them is immaterial.

In the absence of a relevant international standard or interpretation, we have essentially to fall back to general principles, as discussed in the IASB's, 'Framework for the Preparation and Presentation of Financial Statements' (IASB, 1989) IAS 8 requires management (para. 10) to use its judgement in developing and applying an accounting policy that results in information that is relevant to the economic decision-making needs of users and is reliable in that the financial statements:

- Represent faithfully the financial position, financial performance and cash flows of the entity.
- Reflect the economic substance of transactions, other events and conditions, and not merely the legal form.
- Are neutral, that is, free from bias.
- Are prudent.
- Are complete in all material respects.

No indication is given of how the inevitable tension between relevance and reliability is to be addressed. However, the standard continues, in words that clearly have been carefully crafted after much heart-searching, to state that in making the judgement described in paragraph 10, management shall refer to, and consider the applicability of, the following sources in descending order:

1. The requirements and guidance in standards and interpretations dealing with similar and related issues; and
2. The definitions, recognition criteria, and measurement concepts for assets, liabilities, income, and expenses in the Framework.

In making this judgment, management may also consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework to develop accounting standards, other accounting literature, and accepted industry practices, to the extent that these do not conflict with the sources specified above.

One crucial point arising from the above, is *how* we decide whether a particular standard or interpretation does, or does not, apply to a given particular situation. Such a decision is often subjective and debatable in itself. If there isn't an existing 'relevant' standard then the remaining process spelt out by IAS 8 para. 10-12 is again subjective throughout. Management and accountants from different countries will look to different pronouncements, and to different traditions, in making their judgements.

It is apparent from the discussion above that the internal reality of the IASB takes a very particular focus. This focus has two related strands. These are firstly that the IASB takes an investor (i.e. a decision-making) focus, and the second is that it adopts a flexible and judgemental approach. This is not of course to suggest that each and every transaction is considered afresh from first principles. But it is certainly to suggest firstly that whether a specific standard applies to a particular group of like transactions is a subjective and flexible decision, and secondly that if it is concluded that neither it, nor any other standard, applies to the transaction under consideration, then the resulting accounting treatment, specific to this different and presumably relatively unusual situation, is likewise a subjective and flexible decision.

A number of issues relate to this focus. It may, in the general case, imply a focus on current values of some kind (not necessarily fair value in the strict IASB definition). It certainly, by its focus on the large, typically multinational, enterprise and the globally-orientated investor, fails to focus on the needs of small and medium enterprises and of developing economies. It follows from our arguments in section 2 that different 'local' (i.e. national or regional) communities will bring their own (different) internal realities into managing the interface between the local traditional internal reality and the more recently introduced IASB internal reality. France is an interesting and important example.

4. THE INTERNAL REALITY OF FRENCH ACCOUNTING

There are a number of sources available giving a survey of French accounting history and tradition. English language examples include Walton, in successive editions of Alexander and Archer to 2003, successive editions of Nobes and Parker, and Walton, Haller and Raffournier (2003).

However we base our exposition on a recent French source, namely Baert and Yanno (2009). This document is both up-to-date, and apparently influential in the French context. This report of over 160 pages was prepared for the finance and economy commission of the Assemblée Nationale (the lower and more powerful house of parliament) by Dominique Baert and Gael Yanno, both of them members of that assembly. It explicitly aims to increase political awareness, and to encourage political involvement and intervention. It therefore has the additional advantage of being directly and overtly involved in the political process which, as discussed later, seems more part of the problem than of the solution. The following extracts from early parts of the report both give the clear flavour, and raise several issues worthy of comment (for original see appendix 1).

France has a highly centralised conception of accounting. Based on legal principles, accounting constitutes an autonomous branch of law, and the State considers itself as the only body entitled to create accounting rules, even if other users may participate in its creation (see below). This conception, consistent with the State's traditional interventionism in the economy and the necessity to create a platform on which to build fiscal rules, has historically allowed the tax authorities (and to some extent, INSEE [Institut National de la Statistique et des Etudes Economiques - state owned Institute - in charge -inter alia- of the reporting of French economic variables such as the annual Gross Domestic Product, and therefore officially in charge of collecting the necessary data from all the French enterprises] to have a major influence in the creation of accounting requirements. Traditionally these rules are brief, and the French Accounting Plan (PCG) is not distinguished by its precision, leaving to users a large degree of flexibility [but see footnote 6 below].

In contrast, in Anglo-Saxon countries, the accounting regulators operate with a separation of legal and financial matters, and with a genuine independence in the achievement of their mission.

French accounting standards are based on an explicit civil law approach to the business resources, which can be envisaged as the totality of rights and obligations ("patrimony") attaching to a person. Accounting is therefore, traditionally, the numerical representation of this legally-defined "patrimony", founded on the ownership rights of a person and on the

changes in these during an operating period. In a celebrated phrase, “accounting is the algebra of law”⁴ and the French accounting system generally takes the legal characteristics of a situation as the basis of determining the accounting treatment.

Opposite to the legal fiction [sic] of a “patrimony” representing a single integrated set of (net) assets, the IFRS standards seek to reveal the underlying economic substance, that is to say that the accounting should reflect the economic rights, obligations and benefits which are available to an entity. The nature of assets, defined via control over their future benefits, is profoundly changed, and departs from the right of personal ownership. It follows that certain assets defined in legal vehicles as separate from the enterprise can be reintegrated into the balance sheet, or that assets under a hire purchase agreement (and thus not legally belonging to the enterprise) should be included in the assets.

However, while lifting the veil of the legal patrimonial fiction, the IFRS economic approach to accounting appears somewhat biased by its orientation towards investors. Indeed, a single natural economic reality does not exist. As in quantum physics, the characteristics of an object vary depending on the point of view, and there are as many “true and fair views” relevant to an enterprise as there are users of the accounts. The IFRS standards only give one particular economic reality, that which satisfies the information needs of individual investors, but nobody can say that the other users of the accounts will find their requirements there.

Ayoub and Hooper (2009) comment on attitudinal implications towards aspects of this situation (for original see appendix 2).

The third large difference lies in the very structure of IFRS standards, which is different from those in France. IFRS standards have been conceived to avoid a rigid specification of rules, which only permits a too strict application to a business. The principles on which they are based therefore leave much room for interpretation. Now most French accountants are in the habit of following the very precise instructions of the PCG, which is based on the Commercial Code. Thus the preparation of consolidated accounts under IFRS is a problem for certain professionals who say they have not been sufficiently trained (Jopson 2005) [in the sense that they feel they have lost their bearings, they feel disoriented, they ask for a more formal frame, they wish they had been more “taken in hand”].

Marseille (2005) describes France as a country very attached to centralised public-domain authority, but equally very reticent when faced with change.

Thus some of our experts believe that the change has been largely perceived as a supplementary concession to the Anglosaxons, while accepting that France has shown no spirit of openness on this point: “opposition to Anglosaxon concepts is valid in all areas, including that of accountancy. This incredulity about fair value has been cleverly transferred to the political arena to try to destabilise IFRS. Further, the French have

⁴ This revealing phrase, which would surely never be uttered in a common law context, dates back at least as far as Garnier (1947).

understood the strategic character of IFRS accounting, and its increasingly financial and economic character”, as one of them emphasises.

These quotations develop the position that French accounting is significantly legalistic (“l’algèbre du droit”), detailed in its rules, bureaucratic, not pro economic thinking, and not pro Anglo-Saxon. Having said that, two caveats must be noted. The first is that the legalistic approach to the net assets is twice referred to as a fiction. The implications are unclear, as the significance of this “fiction” for French thinking continues to be emphasised. In fact, the statement, widely accepted, that, for example, credit-bail leasing creates an asset not belonging juridiquement à l’entreprise, is simply wrong. As was recognised by Raybaud-Turrilo, (1997), a credit-bail creates the right to use the (tangible) asset, and that right is legally enforceable, i.e. belonging juridiquement à l’entreprise (as an intangible asset), in the fullest sense of juridiquement. As she says, (for original see appendix 3).

It seems clear, from an analysis of different aspects of these contracts, that the formal analysis of the contracts does not allow an understanding of the nature of the operations, this is often in contradiction with the reality of the *rights* and *obligations* of the respective parties... It is therefore imperative to extract the legal substance of the operations and to propose new *legal* analyses to re-establish the coherence rather lost from these contracts. (Raybaud-Turrillo, 1997: 28, emphasis added).

The second point, which is central to our entire philosophy, is the recognition that there is no “natural” economic reality at all, that there are many “true and fair views”, and that that which may absolutely genuinely represent a true and fair view for an investor, may simply be misleading, or useless, for different users and purposes. Our exposition in section 2 above points exactly in this direction. The implications of this point, which the Baert/Yanno report seem not to develop as strongly as they should, are fundamental, and we return to them below.

World Accounting Report (May 2009: 11) states that Baert and Yanno

observe that, to the great indifference of Europe, the Commission decided – in secret, they claim – to require listed companies to produce their consolidated accounts using IFRS.

The suggestion of indifference may be valid, but the charge of secrecy is not, as the Commission clearly signalled its intentions (European Commission 1995, 2000), well before the edict itself (European Parliament and Council, 2002). The process was certainly undemocratic, as national parliaments had no say at all, and the European

Parliament virtually none, but that is a different point. Indeed, such centralised bureaucratic decision-making is not only central to the EU philosophy and *modus operandi*, it is also surely in the French tradition! McDonald (2000: 107) states bluntly that “the European Commission was never intended to fit models of democratic accountability as we might now understand them”. She quotes a comment from an official from an un-named Member State joining the EU in 1995 (therefore not the UK) (2000: 118): “The Commission is childish, male-dominated, very southern and very French”.

No *liberté, égalité, fraternité* nonsense here!

Perhaps more important to our theme here, however, is the move towards IFRS philosophy and regulation within French practice and within the *Plan Comptable Général* (PCG). Baert and Yanno comment as follows (for original see appendix 4).

Further, if IFRS standards are only obligatory in the EU for the consolidated accounts of companies obtaining funds from the general public, i.e. about 7000 groups in Europe of which 1000 are in France, our country has chosen to modernise the PCG, applicable to the individual entity accounts of all companies, converging it towards IFRS. That is to say that through the dissection of this convergence, millions of businesses have seen their accounting environment change considerably, with all the difficulties implied by such changes, not only in the accounting practices, but equally in taxation matters, since, in our country, it is the accounting which determines the basis of company taxation.

Yet, it is regrettable that the decision to converge French accounting law towards IFRS standards – however justified it may be – was the work of the CNC alone, and that the details of this convergence were defined in secret deliberation. Indeed, given its tax, social, economic and legal implications, the process should require that the options are debated, and that guidelines be established by political representatives: on the contrary, the latter were merely restricted to ratifying, after the event, a process decided behind their back. The CNC has thus taken the absence of politics and established a purely accounting direction, aligned as much as possible with IFRS. Without the politics to guard against idiocies⁵, the transition has been made “at the gallop” changing drastically in a few years the practices of millions of businesses. The modernisation of the PCG turned out to be the major part of the CNC working programme around the early 21st century; it was achieved in two ways. For one part, by a specific regulation transposing a single standard (for example regulation 2000-06 for IAS 37 “provisions, contingent liabilities and contingent assets” and, for the other part, a single regulation transposing a large number of standards (for example regulation 2004-06 for IAS 2, 16, 23 and 38).

Regulation 2000-06 of 7 December 2000 relating to liabilities

⁵ A literal translation. But would anybody other than politicians claim that politicians *prevent* idiocies?

The adoption of this regulation introduced into French accounting law a rigorous and precise definition of liabilities. Thus although previously the PCG defined them as “an element within the resources having a negative value to the entity” (former article 212-1 of the PCG), this became “an obligation of the entity with the nature that it is probable or definite that it will provide an outflow of valuable resources, without set-off, or at least an equivalent expectation thereof” (current article 212-1 of the PCG). These different specifications have, *inter alia*, put an end to the abuse, by numerous businesses, of provisions for liabilities and charges, called “big bath” [literally “blood bath”] created on the occasion of a change in management, and designed to falsify the image of the business in a direction favourable to the new team.

It is legitimate to believe that the introduction of “fair value” in the measurement of assets and liabilities, constitutes an undeniable improvement in contrast to the traditional measurement using historical costs: this latter certainly gives a figure in the balance sheet sometimes far removed from the true value. The “fair value” certainly improves the information for investors who are thus given, every three months, a precise measurement of their potential gains and losses, and therefore of the risk profile of the relevant businesses, so permitting a better allocation of investments.

Yet, the other side of the coin is a strong volatility in the values for the assets and liabilities. Because these are fixed by the financial markets, which can have panics, trends, Press over-coverage or “runs”, the profits and the balance sheet of enterprises, and especially of those financial institutions which are stuffed full of financial instruments, give a greater good or bad picture than that which would result from their ordinary activities. When the markets are on the up, the performance improves automatically, on the other hand, when the markets are moving down, the results are reduced in the same way, (and this independently from Top Management economic decisions or the performance of the ordinary activities).These accounting standards tend to disconnect the performance and the valuation of the business from its own genuine activities. This which is anyway a problem may become even more serious when the markets are not working correctly [sic!], as at present.⁶

⁶ Some passages from the report seem to contradict each other : “ Le PCG ne s’est *jamais distingué par sa précision* , laissant aux utilisateurs une large marge d’appréciation” . “ Or la plupart des comptables français sont habitués à suivre *les instructions très précises du PCG* qui est basé sur le code de commerce” . “Le règlement n°2000-06 : l’adoption de ce règlement a introduit dans le droit comptable français *une définition rigoureuse et précise des éléments de passifs, alors qu’antérieurement le PCG se bornait à les définir comme...*”. Thus, to put it simply : Do Baert & Yanno think the PCG was precise or not precise (before the introduction of IAS into the PCG)? We assume that the first quotation is an aberration, an assumption strongly supported by Ayoub and Harper as quoted in the text.

There are a number of reasons which might have influenced the policy of introducing detailed IFRS regulations into the national PCG. One is that membership of IFAC by the French professional accounting bodies automatically accepts the obligation by each body to use its “best endeavours” to encourage the incorporation of international standard requirements into the national system (IFAC, 2006). This seems unlikely to have been a major practical factor. Perhaps more likely, though more nebulous, is a general political pressure, perhaps almost an unstoppable contextual ethos that such changes were inevitable, universal and therefore unavoidable. Certainly all other EU countries were following a similar policy.

In the course of our detailed investigations into IAS37, reported in section 5 below, we discovered a more specific argument, of direct relevance to the Baert and Yanno statements. In an interview with the Chairman of the CNC committee responsible for creating the detail of regulation 2000-06, he stated as follows (for original see appendix 5).

It would seem an aberration if a legal risk is taken into account in two different ways in the group consolidated accounts and in the individual company accounts!; this is why we have put IAS 37 into the PCG with hardly any modifications.

Several points arise from this. It does not explain the timing of the 2000 regulation, 2 years before the 2005 regulation was announced, and 5 years before it was introduced. The Baert and Yanno accusation of proceeding at the gallop (“*pas de charge*”) perhaps has some justification. Secondly, however, if the French do not like the French procedures for adopting and adapting the French regulatory system, then the French have only the French to blame. Secretive, if not mindless, bureaucracy is a long-lasting plague in France, and the French are much affected and weakened by this scourge, which rages also within the accounting institutions. Indeed it seems consistent with much of French daily life as both the authors of this paper have experienced it.

But there is an important third issue, which is of a more direct academic nature. This is that the argument of the CNC spokesman is not correct. To be more precise, it is certainly correct to say that, in the sense of statistical probability, a risk is completely unaffected by the level of entity doing the reporting, i.e. it is independent of the *reporting* context, and independent of the nature and needs of the user group or groups concerned. *But financial statements do not report risks.* They report *financial evaluations of risks.* And these are certainly not independent of the nature and needs of the user group or groups concerned. The statement by Baert and Yanno, already quoted, that there are as

many different true and fair views as there are users of financial reporting is in principle absolutely correct.

To give a highly topical illustration, the European Commission in its 2000 document at footnote 11, stated as follows:

The Commission proposal does not address supervisory issues and the specific information required by supervisory authorities. The implementation of the proposal should not lead to a lessening of the prudential requirements for regulated entities.

In other words, the Commission believes (believed) that IAS are implicitly unsuitable for, and explicitly are not recommended to be used for, prudential regulation by supervisory authorities.

The evaluation of uncertain (risky) liability situations merely encapsulates the point perfectly. An investor needs the likely outcome. A bank manager (and a bank regulator) needs a prudent outcome. The tax authorities need an objective outcome. Different reported numbers are implied. Our analysis in section 2 uses different terminology, and is derived from a different theoretical tradition, but it points in exactly the same direction. In the words of the Alexander and Archer quotation, collective intentionality creates institutional facts, *but only within a particular collective*. In the words of the Baert and Yanno quotation, a particular group of *utilisateurs* will create its own *image fidèle*. SMEs and multi-national groups are different collectives, with different *utilisateurs*. Investors and prudential banking regulators are different collectives, with different *utilisateurs*.

Unfortunately footnote 11 from the 2000 EU document has disappeared, and is not even hinted at, in the definitive 1606/2002 regulation. It seems to have been totally ignored ever since, with well-known disastrous results. For the banking industry to blame the IASB, or fair value reporting, for revealing the effects of its own incompetent management and incompetent regulatory activity is an insult to the intelligence, but the issue is outside our necessary scope here.

To summarise our argument in this section, IASs were introduced, certainly undemocratically, but not secretly, by edict, for the consolidated accounts of listed groups, under valid logical arguments related to meeting the needs of a major, and clearly defined, user group. They have also in various ways been introduced into local GAAP, such as the PCG, into banking regulation by the authorities concerned, and so on,

by choice, although they are not logically likely to be useful for such different purposes. The PCG of the 1980s and 1990s was coherently designed to achieve French-defined objectives (creditor protection, prudent dividend distribution, etc), within the French operational and cultural milieu. Prudential banking regulators had created measurement policies, liquidity ratios, etc, which were coherent with their own objectives (secretive to the point of deliberately lying to depositors about the strength and performance of the banks, but) consistent with their own clear and visible objectives. *Without being legally required to do so*, IASB regulatory thinking has been introduced into these systems. France has *volunteered* to do this, as Baert and Yanno explicitly confirm. So our title is explained and justified. Truly *La France se tire une balle dans le pied*.

It is interesting to relate our analysis to the historical approach taken by Colasse and Standish (1998). In that paper they examine the development of the French regulatory process from 1945 to 1998, proposing four sub-periods. Essentially their argument is that in the 1950's, regulation was more-or-less totally controlled by the State, with the accounting profession having no significant involvement. They refer to this (page 10) as similar to the Colbertism of the absolute Monarchy of Louis 14th. They show that this absolute control has been significantly weakened up to 1998, raising the possibility of "la fin du colbertism comptable" (page 21), although concluding that it is too early to answer "yes" to that question.

In this context, our arguments here clearly show a further strong decline in the role of the state. Regarding the introduction of IFRS for listed group accounts, the loss of power is of course absolute (to Brussels). Regarding the changes in the PCG for "French GAAP", the loss of power, in practice, is highly significant, the CNC being allowed to operate effectively unchecked. The state is perhaps now trying to fight back, as illustrated/represented by Baert and Yanno. Whether the state should be encouraged or discouraged in these attempts is an issue for another occasion (and the same question arises in relation to the arguments at the IASB regulatory level raised by Chiapello and Medjad (2009)). But the scenario is clear, and in that sense our paper updates Colasse and Standish (1998).

A major contribution of this paper is the primary research conducted by one of the authors regarding the interpretation and operation of an IFRS-inspired regulation. The example, already referred to by both Baert and Yanno, and ourselves, concerns the incorporation of IAS 37 into the PCG. We introduce, reveal and review this research in the following section.

5. A CASE STUDY OF FRENCH PERCEPTIONS

Following our exposition of the internal reality of French accounting from a historical and institutional/regulatory perspective in section 4, we now seek to expose this French reality from a practice and operational point of view. Thus, in this section, we show how French enterprises bring their own internal realities into managing the interface between their local traditional internal realities and their operationalisation, on the one hand, and the more recently introduced IASB internal reality on the other. As already indicated, we focus our observation and analysis on the particular case of IAS 37.

Between June 2004 and June 2006 we conducted a field investigation on “How French listed companies actually make their decision when it comes to accrue and comment on their legal risks in the financial statements?”

5.1 Research method

To inquire into this litigation loss contingencies disclosure process we have adopted a qualitative approach based on semi-structured interviews. A qualitative research seemed to us the most adapted method for dealing with this sensitive question. As Daft (1995) pointed out: a questionnaire mailed to a random sample of managers is unfit for a research project which proposes to study a subtle and intangible decision process. In the same manner, disseminating on a large scale mailed questionnaires dealing with litigation loss contingencies and hoping in return numerous and sincere answers didn't seem to be the sensible nor realistic thing to do either.

Thus 22 informants were interviewed (some of them many times) and the time scale of these interviews varied between one and two hours. Each informant was working in a different entity. The prevailing criteria on the choice of respondents was the following:

- selecting people who are witnessing the phenomenon under study. That is, informants who, due to their position, are directly or indirectly involved in litigation loss contingencies disclosure process.
- selecting informants working at different hierarchical levels : directors' assistants for example, in order to gain new insight and not only depend on a director's personal point of view.
- selecting informants with potentially conflicting interests. For example, we thought of the opposition between auditors and lawyers (auditors trying to

disclose as much as possible, whereas lawyers prefer confidentiality). Other potential oppositions have been studied (Auditor / CFO, that is, conservative versus aggressive reporting) and also financial analysts / CFO, company legal department directors / magistrates.

- selecting informants who have acquired a lengthy experience and are well known in the field of finance.

- contacting former members of the “Commission on liabilities” who used to work for the French Accounting Standard Committee (Conseil National de la Comptabilité). These persons have been responsible for the introduction of IAS37 in French law, each representing important stakeholders of accounting disclosures. We decided to adopt a grounded theory method (Glaser & Strauss, 1967) ; selecting each new informant according to the results of previous research interviews.

We describe herewith our sample of interviewees as much as our confidentiality constraints allow. They have requested us not to reveal the sector to which these large listed companies belong. Some sectors may be oligopolistic and this might facilitate the identification of certain groups.

Position of the 22 informants

Internal informants (all belonging to large listed companies in France)

- 2 Chief Financial Officers (Head Office)
- 2 Accounting Procedures Department Directors (Head Office)
- 1 Consolidation Department Director (Head Office)
- 1 Financial Reporting Department Director (Head Office)
- 1 Chief Executive Officer and former Risk Manager (Head Office)
- 1 Legal Department Director (Head Office)
- 1 Law Counsellor (Head Office)
- 1 Chief Financial Officer (800 employees subsidiary), former Financial Chief Officer Head Office assistant.

External Informants (all working directly for large listed companies in France)

- 1 Lawyer responsible for defending several listed companies (former internal Law Counsellor)

- 2 external Auditors
- 2 Financial Analysts
- 1 American Law Counsellor (influential person at the American Corporate Counsel Association)
- 3 external Auditors of several listed companies subsidiaries
- 2 Regulators
- 1 Magistrate at the "Conseil National de la Concurrence" (National Council of Trade Competition)

The (interview) guide content continuously evolved by integrating the questions emerging from previous interviews. For instance, we often aroused respondents' reactions on other interviewees' previously collected opinions. During the course of the interview, some answers stabilized, and we were also able to focus on some other more detailed points. Consequently, given its "made-to-measure" and ever-changing nature, we are unable to provide the interview guide which helped us to obtain all our results, but rather, the reader will find in its generic form the main and most common questions asked to interviewees.

Main questions (in their generic form) asked to informants :

- How is the decision made to accrue a litigation loss contingency and /or to insert a footnote in the financial statement ?
- Who participates in this decision ?
- What are the stages of this decision ?
- Which procedures are implemented ?
- Who are the true and most influential decision makers ?
- Who is responsible for the disclosed information ?
- What is your direct or indirect role in this decision process ?
- What role do the other actors play?
- What political tactics, actors' strategies, power struggle, balance of power, do you perceive in this decision process ?
- What decision criteria is this decision based on ?
- Finally, what haven't I asked that you think I should have ?

Taping was not employed due to the sensitivity of the topic. Although our profitable contact possibilities weren't inexhaustible, we endeavoured to apply a saturation principle as much as we could. Thus sampling was conducted until theoretical saturation was reached or when incremental learning was minimal.

Finally, two difficulties noticeably conditioned our research design. The first difficulty lay in what we call "contact cutsyndrom". Indeed, at no time (during the inquiry) were we allowed to go from one employee to another, that is, benefiting from the contact with the interviewee in order to infiltrate a company or to enlargen our network. We constantly faced the same clearly stated answer, "I don't want other people within the company to know that we have had a conversation on this topic, so, don't ask me to recommend you to another person in the group, nor show your presence at the annual closing time of our provisions files."

The second difficulty lay in the half covert nature of our approach. It was very clear that we certainly couldn't announce the real subject concerning our research project and certainly not over the phone. "Can you talk about your litigation issues and the accounting provisions related to it" is a politically incorrect question. Therefore, an interview was required in person.

We always hid our real research objectives until the moment of our face to face interview. Up until that moment, the research theme serving as a pretext to obtain an appointment was that of a far more general matter, ie: the accounting data production process in listed companies. Consequently, on the day of the interview, all remained to be done, since the challenge was to move from accounting data in general, onto provisions for litigation loss contingencies, in particular.

5.2 Research Results

Two major results have emerged from our study as follows:

- The Chief Financial Officer governs the litigation loss contingencies disclosure process-allowing very little room for corporate law counsellors, lawyers and auditors.
- IAS 37 has a weak influence on the way this key actor (CFO) makes his decision.

5.2.1 CFO governs the litigation loss contingencies disclosure process

The idea of the CFO almost solely governing the disclosure process was rarely announced at first. The question "who actually decides the amount accrued ?" was answered firstly as "there's not a single decision maker but several. Considering the number of stages and procedures that data has to go through before appearing in the financial statements, this decision is obviously collegiate". Nevertheless, once the respondents were put at their ease (by reassuring them of the researcher's university identity and on the anonymity of their comments) the first reactions obtained at the beginning of the interview turned into a much more interesting and drastically different perspective by the end of the conversation.

In this way, we discovered a decision process riddled with informal practices thereby leaving full power to a single actor. This actor, depending on the gravity of circumstances was either

a CEO (exceptional case) or a CFO (usual case). Indeed, many shortcuts and tacit instructions (heard by every one, though never written) have a noticeable effect on the process, giving de facto full power to a single actor.

Shortcuts affecting the decision process supposedly collegiate and continuous all over the year

Last minute trade-offs of provisions for loss contingencies occur at the end of the year, at the same time as consolidated accounts, although these latter are deemed to be the mere reflection of prior closed individual accounts and this in a collegiate manner. (Accounting retreatments are allowed between individual and consolidated statements in cases of distortion between national standards governing consolidated Financial statements, but these distortions, during this period in time, did not exist in the specific case of provisions for litigation loss contingencies.)

Some provisions have more of an end of year nature than others ...At the end of year a CEO or a CFO may do some closure trade offs of certain litigation categories. Frankly speaking, for material lawsuit cases for example, it's not rare that the accruing decision arrives late to the point that is really made in the very last moments of the year... On the other hand usual and unmaterial lawsuits involving relatively small amounts, are managed and recorded in accounting all throughout the year. (a Consolidation Department Director's assistant , Head Office).

Tacit instructions known to all, yet not written.

The informal aspect of the decision process also manifests itself through tacit instructions given by the CFO. These instructions are perceived more than they are actually heard by internal actors, and these instructions strongly condition the outcome of the process: that is, they have a direct influence on the decision on whether to accrue or not a provision:

When a CFO doesn't want to hear about provisions for the year, everybody knows it and acts accordingly...obviously, this is not the kind of instructions that are sent by emails or that appear in memos. (Consolidation Department Director's Assistant, Headoffice).

So, as we have noticed, the informal side of the provision for litigation loss contingency disclosure process can be very important. This domination of informal practices exerts a major effect on the decision power sharing in the process. Far from favouring a larger power sharing, these informal practices are in fact giving full power to a single actor. The concentration of power on a single actor was also directly confirmed by interviewees: after an hour's worth of interview for some of them or during a second face to face interview for others the answer to the question "who actually decides ?," became more apparent:

The CFO leads the way when the question is asked whether to disclose or not a litigation... (a Consolidation Department Director's Assistant at the Head Office)

When a litigation appears, I try to react in real time and in the following days I contact my operational staff, and the lawyer with whom we usually work, but the decision of what amount to accrue, and the decision to accrue or not, I make it on my own. (Subsidiary's CFO)

Nevertheless, these comments require a final adjustment to reflect as truly as possible the accurate discussions collected. Indeed, depending on the seriousness of the situation, its critical aspect, the real action of decision may switch identity in some exceptional cases .

In extremely serious situations, where a lawsuit is likely to have a sensational and longlasting impact on a company's image, the CEO tends to centralise full power and all the functions (of the different company's departments).He takes the place of Corporate Communication Chief Officer to personally address the press, and substitutes for the CFO in order to decide which accounting solution to give to the lawsuit in the Financial Statements . In fact, in moments of crisis the CEO appropriates full power again by recentralizing all functions :

When there's a material environmental affair with human lives at stake (casualties) or when there is an unfair problem of competition and when an over coverage in the press describes it as a scandal, that is, when the consumer feels betrayed, let's say, a price arrangement between companies, then in this case the CEO and not the CFO takes control . He, on his own, assesses the litigation financially. In the other cases, where a company's reputation and image aren't challenged, the CFO makes the decision. We call that "controlled delegation", but frankly speaking, the CFO makes his decision alone..(a Consolidation Department Director's Assistant at the Head Office)

CFO leaving little room for corporate law counsellors

In principle, we could expect that internal law counsellors (wherever they may be, at subsidiary level or Head Office) play a great part in litigation assessment, at least as important as the CFO since they are the persons (in the company) who know the case the best. Certain interviews at the beginning confirm this expectation, and according to some interviewees, this idea flows from “common sense”.

But, thorough and deep examination of this question has revealed another reality. **Indeed, a CFO seems to be able to impose his litigation assessment in all circumstances.** Several clues make us think this :

-In some companies the dominating relationship imposed by the Financial department on the legal department is even institutionalised : two of the companies which we studied have a legal department which is situated below the Financial department in the organisational chart. Here, as we can see, the principle of directors being independant is not even respected in the chart. Therefore, in these conditions, how can we imagine that Finance Management might not exert some kind of pressure on the law department when evaluating a litigation?

-In another group, where the legal department is not subordinate to the Financial department but directly tied to the CEO (at least in the organisational chart) the informal Financial Department's domination is even mentioned as such without any sign of hesitation:

When it is about a litigation description in the footnotes, the law counsellor puts pen to paper but he is always under the CFO's control. (a Consolidation Department Director, Head Office)

We were told other cases where law counsellors weren't even consulted. (That is, the legal profession was given the cold shoulder.)

Accounting and Financial Chief Officers justify the fact that law counsellors are pushed aside when assessing provisions, as follows: Law / Financial collaboration is said to be desirable

but often impossible in practice, and consequently, but unwillingly, they preclude law counsellors from the provisions elaboration process.

The first argument put forward is that of two incompatible reasoning modes, qualitative and quantitative, conflicting with each other, without any results, and isolating the CFO in his quantitative assessment task of litigation issues. This first reason sounds like “cognitive barriers” between professions formerly evoked by Dougherty (1992).

The second argument is the little interest showed by most law counsellors in accounting issues. This lack of interest forces Financial Officers to work all alone.

Law counsellors have only one single idea in mind: the defense of the case, and their collaboration with lawyers. Their only concern is to know whether we disclose or not. They are systematically urging us not to disclose. They are afraid of being disturbed in their defense strategy. But the question of what amount should be accrued doesn't interest them at all ... Besides, there's no use going to consult them for whatever evaluation or amount.

Law counsellors or more generally the law profession (including lawyers) never attend accounting debates at the CNC (Conseil National de la Compatibilité, The French Accounting standard Board) and what is more surprising is : the law profession never participates in the debate even when it's time to give a ruling on a relatively long text supposed to rule litigation loss contingencies, assessment and disclosure.

This “under-representation”, not to say the least, absence of representation from the legal profession within accounting institutions doesn't appear to be an isolated and only a typical French issue. As far as we know, on an International level, only the American Bar Association and the GC 100 (Group for general counsel in the UK) mobilised to send a comment letter to IASB regarding IAS37 Reform project. (ED IAS37).

Later in the interviews another reason was indicated to explain the blatant lack of collaboration between the accounting and the law professions.

When the CFO asks the legal department Director or even the Lawyer: “What is the amount of damages we are likely to spend and when will it be spent?”, it amounts to asking: “When and for how much are you expecting to fail?” The

very nature of this question is not supposed to make these legal actors at ease and in return we cannot expect to obtain very useful and relevant answers.

CFO leaving little room for lawyers

Like internal Law Counsellors, it might be expected that lawyers play a very active role in the financial assessment of litigations. As they are in charge of the defense strategy they can be seen as the most informed people regarding the case, and its evolution. These lawyers can be considered (at first sight) as actors to be reckoned with, when assessing possible damages outcomes, their probabilities, and the timing of the cash outflow. In reality Lawyer's role is marginal when addressing these questions. A Subsidiary CFO's comment is enlightening:

The only work we await from lawyers is the defense case, for the rest it is our own business.

All things well considered, it looks as if this obvious power imbalance between a CFO and lawyers concerning litigation assessment in the financial statements is a satisfying situation for both actors. Indeed, in this way, lawyers flee responsibility concerning an evaluation in the Financial statement and the CFO appreciates the leeway the latter is giving him:

Lawyers may be asked by the company what are the risks? But lawyers will never say anything like we will win for sure, and won't even dare give any written assessment of whatever probability regarding the outcome of the case. Their aim is to stay as neutral as possible by telling "here is what happened for similar cases and that's it". (a Lawyer)

Does the lawyer give an assessment of the time when damages are likely to be disbursed? No, the only certainty is the next step in the judicial proceeding, but as Lawyers we never pronounce at the time when something has to be paid. (a Lawyer)

CFO leaving little room for external auditors

Concerning litigation loss contingencies disclosure process, external auditors represent an almost ineffective force of opposition. Indeed, auditors' means of investigation are very limited: they can only rely on:

- The circulation of information between lawyers.
- The examination of lawyer's fees and other billed elements to try to detect some potentially hidden law suits.
- Management letters
- "Reverse" management letters as the following states:

Now, as an external auditor, if we are not very confident in the explanations given by management, we will demand a "reverse management letter: such as: I have asked you this and this regarding your responsibility or liability in the Case, and your answer has been the following...,and we try to get these explanations signed (an external auditor)

- The Press

Finally, as a 30 year- experienced external auditor stated:

our last resort is the circulation of information between lawyers.

Yet, this mode of investigation is considerably weakened by the "frosty collaboration" which exists between both professions. This "frosty collaboration" is due to historical conflicts and rivalries opposing both professions, but is also due to objective conflicting interests towards financial disclosure. Auditors would rather disclose everything as soon as possible, whereas lawyers do prefer confidentiality in all circumstances.

We note that the "frosty collaboration" between lawyers and auditors seems not to be limited to a specifically French quarrel. As Amhowitz (1987) humorously said:

(in the USA) ... the early tax rates were so low that the subject was considered beneath the dignity of lawyers. For this reason, accountants originally occupied the field, it was not until the rates increased to a degree that made tax practice lucrative enough to engage the attention of the lawyers that they discovered, to their horror, that tax practitioners in the accounting profession were engaged in the unauthorised practice of law(...) the two professions have also quarrelled in recent years over the subject of

contingent liabilities. A long and somewhat acrimonious exchange of views has led to what passes for a solution, with the accountants frustrated by the rock of the attorney client privilege.

Therefore if the auditor cannot really rely on lawyers, he may probably resort to an external law counsellor for advise who could help him by providing him with an in-depth understanding of the litigation. But even if we consider the question of who will pay for these extra fees, the most essential question as some respondents indicated, is the relevance of such a decision.

Regarding this, interviewees' answers are similar to Krogstad, Taylor and, Stock 's (2002) point of view, when they argued that

auditors generally cannot turn to other legal experts (including their own counsel) because of the inability of such experts to access confidential details about the litigation and their lack of knowledge about how the client's lawyers plan to defend against the action.

Finally, some other respondents have also specified that resorting to an external legal expert for advise should be interpreted as the will of Auditors to be legally irreproachable (legal cover), rather than wanting to discover the truth by all means.

Auditor's investigation means are weakened by an accounting standard leaving a large open space for opportunistic tactics:

In fact, auditors' control is all the more weakened as the standard ruling provisions for litigation loss contingencies is very vague.

This vagueness permits plenty of possible opportunistic tactics...

The resource outflow probability depends also on the probability of liability in this damage:

Then, if the company denies any liability, is it enough to mention nothing, even in the footnotes?

Yes, obviously, as resources outflow probability is becoming less than likely there will be nothing to mention, not even in the footnotes...and that's the real problem (an Auditor)

In the standard's text, it is indicated that as soon as the total amount of provisions for litigation loss contingencies becomes material, companies have to isolate this amount from the rest of the provisions. But the term "material" is not defined anywhere, so how do you manage to make this rule respected when facing this problem?

We are totally disconcerted. (an auditor)

Equally, as other auditors have acknowledged more or less optimistically, the combative assertive tone with which a litigation case is described in the financial statement is hardly "standardised", this leaves in reality a large leeway for CFOs and throw auditors into confusion.

Auditors' repression means: theoretically efficient but impracticable.

If the accounting standard on litigation loss contingencies hasn't any effective disciplinary power, then as a last resort, auditors may wave the threat of a refusal or that of an audit qualification. But in practice, qualifications and a fortiori refusals hardly ever happen.

In concrete terms an auditor is faced with a tricky trade off or even a dilemma. On the one hand, there's a risk or even certainty in the very short term of irritating the client, and on the other hand, there's a long term risk that shareholders will realize that at the time that the auditor checked the financial statements, a qualification should have been made...

What supplementary means does the auditor have when, even covered by a management's letter, he feels he still doesn't know the truth about a material litigation issue? Theoretically, the auditor may wave the threat of a reservation but in practice, in France, as an acknowledged regulator this solution is hardly ever considered or even used.

As an auditor, what kind of arguments can you use when negotiating with the client? When we think that the accounting option retained is not a conservative one, we never wave the threat of a refusal but we simply insert an observation in our audit report indicating the fact that litigation may lead to outcomes very difficult to measure and predict now.

Nobody will reproach you for disclosing an observation whereas with a qualification or even worse a refusal, the relationship with your client becomes very tense. (An auditor)

These conclusions on CFO's domination in the disclosure process would be worth being supplemented by two remarks.

1-The fact that responsibility for the disclosure of accounting information is distributed very unequally among actors and could largely explain the reason for a CFO's omnipotence.

Indeed, there is strong evidence that the accountability towards financial disclosure and then towards financial statement readers is shared very unequally (rightly or wrongly) between the different protagonists in the disclosure process. Obviously, despite management letters, confirmation letters, making each actor in the process "co- responsible" for the financial informal disclosure, the feeling of being held, eventually, accountable for the quantitative and qualitative assessments of litigation disclosures in the financial statements before a court, is changing dramatically according to the interviewee's position in the process... Thus lawyers and internal law counsellors don't feel responsible at all for the disclosed provisions in the financial statements.

But even auditors seem to think that:

Anyway, litigation assessment is done under the influence of lawyers. We are not able to make a judgement based on the statutes or even on the facts as legal professionals would do, only lawyers can evaluate, what is likely to be paid...(an auditor).

Thus, if a CFO has so much power in the process it is presumably because he is viewed as the most accountable person for the disclosed information regarding litigation loss contingencies; consequently the other actors (lawyers, law counsellors, auditors) allow him, without any reluctance, to take all the necessary initiatives he desires.

2- The line of argument concerning the vagueness of a litigation may suit everybody? (Except shareholders).

Some interviewees indicate clearly that uncertainty characterising a litigation may be strategically exploited by auditors. As long as this uncertainty can be justified and is tenable before investors, it sometimes allows auditors to continue to satisfy their client (by accepting

his aggressive accounting solution) without engaging any further their own responsibility or reputation.

Therefore, vague rhetorical speech might suit every actor in the process.

5.2.2 IAS37 has a weak influence on the way the CFO makes his decision

IAS37 demands the use of a specific probabilistic reasoning which is hardly employed

The French accounting standard on liabilities (which is a mere translation into French law of IAS37) prescribes that the probability of resources outflow relative to litigation be calculated, firstly by assessing the three following probabilities:

- The probability of the existence of the damage.
- The probability of the company's liability for the damage.
- The probability of staking the entity's name in the damage. (i.e.: probability that a claim be made).

The conjunction of these three probabilities should lead to the determination of the probability of an outflow of resources.

In other words: the matter is about answering the question: Is the resources outflow probable? In the same manner, the assessment of the amount likely to be paid (relative to litigation) implies in turn that one resorts to a probability calculation. Finally, concerning the timing of the cash outflow (corresponding to damages), IAS37 (§85) prescribes that for individual material provision for loss contingencies, this timing should be mentioned. In this way, companies are explicitly invited to think about the probability of the timing of the expense.

This list of standard prescriptions accounts for the very significant room that IAS37 leaves for probabilistic reasoning. Yet, these prescriptions are not accepted very well in the effective decision behaviour of the French CFO. Here are some comments:

Do you resort to probable calculation when you are assessing the Financial probable outcome of the litigation?

- No, more often than not we put zero or the maximum amount, that is, the amount claimed by the opposing party, we don't give estimates.(Financial Reporting Department Director, Head office).

Companies don't want to bother with the calculation of probability of the claimed amount, they accrue the maximum amount given judicial vagueness, calculating a probability would be complicated that's why companies accrue the total amount when a provision is needed.(Lawyer).

And what about estimating the timing of the cash outflow, do you discuss it so as to evaluate it as accurately as possible?

Honestly this is totally fuzzy! That's the reason why we never resort to actualisation when we deal with provisions for litigation loss contingencies. You know, there are so many uncertainties, especially when we are at the beginning or at the early stages of the proceedings. At this time it would be nonsense to give an estimation of the date of payment (Financial Reporting Department Director, Head office)

These quotations seem to enhance the idea of an apprehension of risk (regarding litigation). It resembles a layman's approach more than an expert's approach. The expert is supposed to take into account, in an equal manner, the probability of occurrence of a damaging event and the seriousness of its consequences, whereas the layman approach is supposed to neglect this first aspect of calculation (Perretti – Wattel 2001).

IAS37 demands to resort to sequential reasoning, hardly applied.

A decision tree is given in IAS37 's appendix. This decision tree is designed to serve as a guide to decide whether or not a provision for loss is required. This decision tree prescribes a strict sequential reasoning with which every preparer should conform and integrate (when making his decision regarding a risky event.) In particular, the reading of this tree implies that one asks oneself three major questions by respecting the following strict order :

1-Is Entity's obligation towards a third party probable at the balance sheet date?

2-Is the resources outflow probable at this same date?

3-Can the estimation of the amount be assessed reliably?

The strict hierarchy imposed throughout these questions doesn't seem to be applied in practice as a 30 years experienced auditor explains:

The calculation of probability is absent in their reasoning. Indeed, they almost often start with what they have decided to disclose in the Financial statements and at the very end they may answer the tree questions by reading them back . In fact, the CFO sets the target and we, as auditors, make him answer the tree questions afterwards.

We don't treat tree decision questions one after the other, we consider them at the same time. (CFO, Head office).

From a cognitive point of view, these comments seem to strengthen Witte's conclusions (1972) p.180 since according to him.

Human beings, cannot gather information without in some way simultaneously developing alternatives. They cannot avoid evaluating these alternatives immediately , and in doing this, they are forced to a decision. This is a package of operations.

5.3 Discussion of interview results

From a standard point of view, our research results give cause for concern.

First of all, the lack, not to mention, the absence of collaboration between lawyers, law counsellors and CFOs, contradicts with the importance of legal judgment granted by the IAS 37 standard (and ED IAS37). Reading the illustrative cases given in the Appendix of these two texts, one can gauge the strong determining role left to lawyers. In this respect, IAS37 seems very unrealistic ... (at least for French cases)

Secondly, the lack of probabilistic reasoning when assessing litigation loss contingencies should concern IASB's standard-setters : IAS37 probabilistic prescriptions is not a relevant decision guide. This is all the more worrying as probabilistic calculation is due to play a growing part in the future. The IAS37 Reform Project (EDIAS37) when it eventually becomes final, seems likely to require consideration of a complete distribution concerning possible outcomes, even the most unexpected, and to attribute to each of them an occurrence probability.

In this new framework, the accrued amount should correspond to the expected value of the distribution and not to the best estimate anymore (IAS37) or to the most likely amount (French Rule). Respondents interviewed on this issue are therefore very sceptical:

Does the project of Amendments to IAS37 fit in with the way you are determining your accounting solutions relative to litigation loss contingencies ? : Not at all, this is even a revolution. The rule with the best estimate was ok ,but then again, ...but their story of an attribution of probabilities to each possible amount of damages is against nature. We are not used to thinking of all possible scenarios and especially when they are very unlikely. We have to invent them ! As I told you, we think of one or maybe two scenarios when assessing a litigation loss contingency but not as a whole distribution !
(Consolidation Director's assistant Head Office)

With IAS37 current rules, what matters is the "more likely than not" test.

But now we have to imagine a whole distribution and then determine the expected value.

Well, that's a different intellectual exercise. If you believe in probabilities... why not ? (Regulator).

These latter opinions tie up with Kahneman & Tversky's (1982: 518)) earlier suggestions. According to these authors, assessment of uncertainty by people relative to the occurrence of probability of a future event (when this probabilistic reasoning exists) is generally apprehended in a singular and not in a distributional mode:

We have conjectured that people generally prefer the singular mode in which they take an inside view of the causal system that most immediately produce the outcome, over an outside view which relates the case at hand to a sample chart (distributional mode). Our planning example illustrates this preference for the singular mode.

Thus, our Field study reveals the accounting behaviour of French listed companies when they are confronted with legal risks. This study illustrates the gap existing between standard prescriptions and their actual practice. The internal reality of the traditional French thinking and practice is different from that of the imported IASB regulations. The interpretation and application of the "new" PCG requirements is significantly influenced by the traditional, local, internal reality.

6. DISCUSSION AND CONCLUSIONS

There are three major elements to this paper. In section 2 we provide a brief overview of some important conceptual issues relating to the function of financial reporting. Accountants are trying to communicate a transparent picture – but of what? We argue that the “what” is socially constructed, and becomes an intersubjectively constructed social fact *within a community which agrees to accept it*. But not beyond that community. Related to this is the problem of communication and language, as the meaning of words is community-specific (both as to time and as to space). So proposed accounting regulations from community A may be neither understood, nor accepted (whether understood or not), in community B.

Section 3 gives a short outline of the internal reality of the IASB “community”, as a context and contrast for our more substantial investigation of the internal reality of the French “community” in section 4. We show that these two internal realities are indeed significantly different, so difficulties of cooperation and coordination are *a priori* to be predicted. But France has *chosen* to incorporate vast amounts of IASB regulation, despite the original IASB cultural baggage which inevitably comes with it, through a process *chosen* by France itself. Problems, and objections, are now large. But the whole scenario is predictable; hence our title concerning a shot in the foot.

In section 5 we present important primary data concerning the attitudes and motivations of leading actors (mainly CFOs but also regulators and others), in attempting to apply a strongly IASB-oriented regulation in the French context relating to a particularly difficult area, i.e. provisions and contingencies and IAS 37. We provide evidence that the CFO in practice usually takes the decision about what to provide and reveal, based significantly on what we might call ‘political’ grounds, and not following the IASB ethos inherent in the post-2000 PCG requirements. This evidence is consistent, at the operational and practical level, with the differences and tensions illustrated in sections 3 and 4, and with our philosophically based propositions of section 2.

The predictability of, and logical rationale for, differences and difficulties indicates that talk of an Anglo-Saxon plot is unfounded. Perhaps such talk is intended to provide a smoke-screen to hide the existence of, and the at times catastrophic results of, the undemocratic decision-making at the EU level, as well as at the French internal level (and even perhaps at the individual listed company level where the CFO often operates alone).

There is an old saying in English, or more accurately in American, which is not the same thing: if it ain't broke, don't fix it. We might suggest a parallel proposition: if it won't work, don't do it. But instead we have *la balle dans le pied*.

APPENDIX 1

La France a une conception régaliennne de la comptabilité. Fondée sur des principes légaux, la comptabilité constitue une branche autonome du droit, qu'il appartient à l'État d'édicter seul, même s'il laisse d'autres utilisateurs participer à son élaboration (voir *infra*). Cette conception, conjuguée à la tradition interventionniste de l'État dans l'économie ainsi qu'à la nécessité de disposer d'un substrat comptable permettant d'asseoir la réglementation fiscale, a donné historiquement un pouvoir déterminant à l'administration fiscale (et, dans une moindre mesure, à l'INSEE) dans l'élaboration des normes comptables. Traditionnellement, celles-ci sont sommaires et le Plan comptable général (PCG) français ne s'est jamais distingué par sa précision, laissant aux utilisateurs une large marge d'appréciation.

À l'inverse, dans les pays anglo-saxons, les normalisateurs comptables disposent de l'autonomie juridique et financière et d'une réelle indépendance dans l'accomplissement de leur mission.

Les normes comptables françaises ont une approche très civiliste du patrimoine qui peut être défini comme une universalité de biens, actif et passif, attachée à une personne. La comptabilité est donc, traditionnellement, la représentation chiffrée du patrimoine juridique, fondée sur le droit de propriété d'une personne et de l'évolution de celui-ci au cours d'un exercice. « *La comptabilité est l'algèbre du droit* », selon une formule célèbre, et le droitcomptable français s'appuie généralement sur la forme juridique d'une opération pour déterminer les modalités de son traitement comptable.

À l'opposé de la fiction juridique d'un patrimoine représentant une unité de biens, les normes IFRS s'efforcent de révéler la substance économique sous-jacente, c'est-à-dire que la comptabilité doit refléter les droits, obligations et avantages économiques qui sont à la disposition d'une entité. La nature des actifs, définis par le contrôle de leurs avantages futurs, en est profondément modifiée, et s'éloigne du seul droit de propriété. C'est ainsi que certains actifs titrisés ou logés dans des véhicules juridiquement séparés de l'entreprise peuvent être réintégrés au bilan ou que les actifs faisant l'objet d'un crédit-bail (et donc n'appartenant pas juridiquement à l'entreprise) doivent être intégrés à l'actif.

Cependant, tout en levant le voile sur la fiction du patrimoine juridique, l'approche économique de la comptabilité qui est celle des normes IFRS apparaît quelque peu biaisée par l'orientation de celles-ci vers les investisseurs. En effet, il n'existe pas une réalité économique par nature. Comme en physique quantique, les caractéristiques d'un objet varient selon le point de vue, et il y a autant « *d'images fidèles* » pertinentes de l'entreprise que d'utilisateurs de la comptabilité. Les normes IFRS ne donnent donc à voir qu'une certaine réalité économique, celle propre à satisfaire les besoins d'informations des seuls investisseurs ; mais rien ne dit que les autres utilisateurs de ces normes y trouveront leur compte.

APPENDIX 2

La troisième grande différence est liée à la structure-même des normes IFRS, qui n'a pas d'équivalent en France. Les normes IFRS ont été conçues pour se défaire des règles spécifiques trop rigides qui ne permettraient qu'une mise en place trop stricte dans les entreprises. Les principes sur lesquels elles sont fondées laissent ainsi une large place à l'interprétation. Or la plupart des comptables français sont habitués à suivre les instructions très précises du Plan Comptable Général (PCG), qui est basé sur le Code de Commerce. Ainsi, la préparation des comptes consolidés selon les normes IFRS pose problème à certains professionnels qui disent n'être pas suffisamment cadrés (Jopson, 2005).

Marseille (2005) décrit la France comme un pays très attaché à l'autorité centrale et au domaine public, mais également très réticent face à tout changement.

Ainsi, quelques uns de nos experts estiment que ce changement a été largement perçu comme une concession supplémentaire aux anglo-saxons, tout en admettant que la France a manqué d'esprit d'ouverture sur ce point : « *l'opposition aux concepts anglo-saxons est vraie dans tous les domaines y compris dans la comptabilité. Cette incrédulité vis à vis de la juste valeur a été relayée de manière politiquement habile pour essayer de déstabiliser les IFRS. De plus, les français ont pris conscience à l'occasion des IFRS du caractère stratégique de la comptabilité et de son caractère de plus en plus économique et financier* », souligne l'un d'entre eux.

APPENDIX 3

Il apparaît clairement, à l'issue d'une analyse de différents aspects de ces contrats, que les analyses formelles des contrats ne permettent pas de comprendre la nature des opérations, qu'elles sont souvent en contradiction avec la réalité des *pouvoirs* et des *obligations* respectifs des parties... Il est par conséquent impératif de dégager la substance juridique de ces opérations et de proposer de nouvelles qualifications *juridiques* pour rétablir la cohérence quelque peu perdue de ces contrats... (Raybaud-Turrillo, 1997: 28, emphasis added).

APPENDIX 4

De plus, si les normes IFRS ne sont obligatoires dans l'Union européenne que pour les comptes consolidés des sociétés faisant appel public à l'épargne, c'est-à-dire environ 7 000 groupes en Europe dont 1 000 en France, notre pays a choisi de moderniser son Plan comptable général (PCG), applicable aux comptes individuels de toutes les sociétés, en le faisant converger vers les normes IFRS. C'est dire que par le biais de ce processus de convergence, ce sont des millions d'entreprises qui ont vu leur environnement comptable changer considérablement, avec toutes les difficultés qu'implique un tel changement, non seulement dans la pratique comptable mais également en matière fiscale puisque, dans notre pays, c'est la comptabilité qui détermine l'assiette de l'imposition des sociétés.

En revanche, il est regrettable que la décision de faire converger le droit comptable français vers les normes IFRS – aussi justifiée qu'elle soit – ait été l'œuvre du seul CNC et que les modalités de cette convergence aient été définies dans le secret de ses délibérations. En effet, par ses conséquences fiscales, sociales, économiques et juridiques, ce processus aurait mérité que ses options soient débattues et qu'une ligne directrice soit fixée par le politique ; au contraire, celui-ci s'est borné à entériner *a posteriori* un processus déclenché en dehors de lui. Le CNC a ainsi comblé l'absence du politique et défini une ligne directrice exclusivement comptable, l'alignant autant qu'il est possible sur les IFRS. Sans garde-fou politique, l'alignement s'est ainsi fait au « pas de charge », bouleversant en quelques années les pratiques de millions d'entreprises.

La modernisation du PCG a constitué l'essentiel du travail du CNC au tournant des années 2000 ; elle s'est réalisée selon deux modalités : d'une part, un règlement spécifique transposant une seule norme (par exemple, le règlement 2000-06 pour la norme IAS 37 *Provisions, passifs éventuels et actifs éventuels*) et, d'autre part, un règlement unique transposant un grand nombre de normes (par exemple, le règlement CRC 2004-06 pour les normes IAS 2, 16, 23 et 38).

– *Le règlement n°2000-06 du 7 décembre 2000 relatif aux passifs*

L'adoption de ce règlement a introduit dans le droit comptable français une définition rigoureuse et précise des éléments de passif. Alors qu'antérieurement, le PCG se bornait à les définir comme « *un élément du patrimoine ayant une valeur négative pour l'entité* » (ancien article 212-1 du PCG), il s'agit désormais d'« *une obligation de l'entité à l'égard d'un tiers dont il est probable ou certain qu'elle provoquera une sortie de ressources au bénéfice de ce tiers, sans contrepartie au moins équivalente attendue de celui-ci* » (actuel article 212-1 du PCG). Ces précisions complémentaires ont, entre autres, mis fin à l'abus, par nombre d'entreprises, des provisions pour risques et charges, dites provisions « bain de sang » passées à l'occasion d'un changement de direction et destinées à fausser l'image de l'entreprise dans un sens favorable à la nouvelle équipe.

Il est légitime de considérer que l'introduction de la « juste valeur » dans l'évaluation des actifs et des passifs constitue un indéniable progrès par

rapport à l'évaluation traditionnelle au coût historique ; cette dernière figeait en effet dans le bilan des entreprises une valeur parfois très éloignée de leur valeur réelle. La « juste valeur » améliore donc l'information des investisseurs qui disposent ainsi, trimestre après trimestre, d'une évaluation fine de leurs plus ou moins-values potentielles, ainsi que du profil de risque des entreprises concernées, permettant ainsi une meilleure allocation des investissements.

La contrepartie, c'est cependant une forte volatilité de la valeur des actifs et des passifs. Parce que celle-ci est fixée par des marchés financiers qui peuvent connaître aléas, passions médiatiques ou « bulles », le résultat et le bilan des entreprises – et en particulier celui des institutions financières qui sont gorgées d'instruments financiers – découlent plus de la bonne ou mauvaise orientation de ceux-ci que des résultats de la gestion ordinaire de leur activité. Lorsque les marchés sont à la hausse, le résultat augmente mécaniquement ; à l'inverse, lorsque les marchés sont à la baisse, le résultat se réduit dans les mêmes proportions, quelles que soient les décisions de gestion des dirigeants ou la performance de l'activité ordinaire. Ces normes comptables aboutissent à déconnecter les résultats et la valeur de l'entreprise de son activité propre.

Ce qui est déjà un problème en soi peut devenir encore plus grave lorsque les marchés ne fonctionnent plus correctement, comme actuellement.

APPENDIX 5

Il serait aberrant qu'un risque juridique soit pris en compte de deux manières différentes dans les comptes consolidés du groupe et dans les comptes sociaux individuels!, c'est pourquoi nous avons intégré IAS 37 au PCG sans presque rien modifier.

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