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Accounting and *Volksgeist* – Territorial Claims on Accounting Regulation

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Abstract. In this paper, it is argued that international diversity in the rules governing corporate accountability is a function of the desire to preserve local jurisdictions by maintaining national distinctiveness. Successive attempts at regulatory harmonisation in Europe have met considerable resistance, starting with Savigny's appeal to 'the spirit of the people' (*Volksgeist*) and ending with the notion of 'subsidiarity'. In this paper, territorial claims on regulation are explored in the context of the rules governing asset revaluation, where there are still almost as many required methods of accounting in the European Union as there are member states. The paper rejects the conventional explanation that such differences are culture-bound, and instead suggests that the continued existence of national rules in accounting reflects the pursuit of autonomy by individual states and the self-interest of national regulators.

1. Introduction

Regulation tends to be seen primarily as a national concern, yet in accounting the international migration of its governing rules appears to have been pervasive. Indeed, amongst the various forms of regulatory migration in the area of accounting are those arising from colonisation, harmonisation, voluntary transplant and, less directly, from the resolution of conflict between national jurisdictions. The experience of importing and exporting accounting regulations has been documented by Parker (1989) and the general case in favour of regulatory development through legal transplant has been argued by Watson (1974). Yet it is not necessarily the case that similarities between rules should be attributed to the process of borrowing from other jurisdictions. An alternative explanation could be that, in resolving universal problems, regulatory systems in different countries merely react in a similar fashion, whilst another line of reasoning would disregard the possibility of legal transplant on the basis that law is as peculiar to a society as its language.

In summary, a comparative perspective on accounting regulation reveals the paradox that, whilst the rules of accounting lend themselves readily to transplantation from one jurisdiction to another, at the same time a kind of false consciousness

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appears to surround the careful preservation of control over rule-making within each national jurisdiction. A greater understanding of these territorial claims over accounting regulation is warranted, including the appeal to self-determination in preserving local jurisdictions and the role of defensive sentiments in maintaining national distinctiveness. In this paper, we trace this paradox back to the early development of accounting regulation and then, with regard to the particular issue of valuation, compare the development of existing regulations in a number of Western European countries with a view to understanding the countervailing forces of international migration of accounting rules and their national legitimation.

2. Accounting Regulation and the Search for National Distinctiveness

At the end of the eighteenth century, Europe entered a period of great turbulence during which time its political structure was shattered. The new states which emerged required new laws, and the writing of such laws was able to contribute in turn to the construction of nationhood itself. Interestingly, the politics of national distinctiveness in which law-making was able to play a key role took place against a backdrop of attempted European integration which, although a failure at the time in military terms, was eventually to be far more successful in the context of the emergent capitalism. The French revolution is often presented as the catalyst for these events, but it is also likely that the expansionist rule of Napoleon was the direct cause of the resurgence of national identity throughout Europe. Indeed, not only was the attempt to enforce European integration a military failure, its immediate effect was to attach new value to traditional customs and local cultures in reaction to the rationalism and universalism with which Cartesian France was then associated (Pearson 1994).

Nowhere was this rational and universal approach more evident than in the new law of France which had, in addition to its deductive reasoning, a political agenda that entailed the dismantling of the territorial division of the country and the removal of the feudal regime. Indeed, within months of the attack on the Bastille in 1789, the French assembly had decreed the juridical unity of France. However, the great project of unifying private law in the *Code Civil* went through three unaccepted drafts in the ten years prior to Napoleon taking power in 1799, and it was only after considerable redrafting and the removal of political opposition that the civil code was finally enacted in 1804. A similar hiatus occurred in the case of commercial law, for it was soon after the revolution that the privileges of monopoly granted to corporations and trade associations by the Crown were repealed and free trade was introduced, and yet it was not until 1807 that a new *Code de Commerce* was issued through the offices of Napoleon's *Tribunat*.

In some respects, the commercial code was far less radical than the civil code, as a previous *Ordonnance de Commerce* issued in 1673 (*la loi Savary*) had already laid down regulations which were applicable throughout the country. However, it was the *Code de Commerce* of 1807 which introduced the *Société Anonyme*, the ‘anonymous’ corporate form which made explicit the potential separation of ownership and management and in which the liability of shareholders was limited to the amount of risk capital invested. Moreover, the commercial code also specified that accounting records (or, to be precise, ‘*la comptabilité regulièrement tenue*’) could provide legal evidence of business transactions and, for the first time, referred to financial statements, both a *bilan* and a *tableau des profits et des pertes*, although only in the context of bankruptcy (Mikol 1995).

The codified law of France was established in several European countries in the ensuing period, but its implementation followed different patterns. For instance, as the Belgian provinces and the territories to the West of the Rhine had already been incorporated into France, all codified law came into force there automatically. In contrast, in the Netherlands where Napoleon had forced the Dutch to accept his brother as king in 1806, a version of the French codified law was enacted with adaptations to Dutch legal practice. After the territory was annexed in 1810, the codified laws were reenacted in their original form, including the commercial code. The French codified law also entered much of Italy in the train of Napoleon’s armies, and it was adopted in a number of principalities in the Rheinbund, a confederation which excluded Prussia and Austria and which was established by Napoleon as a client state in 1806.

The first codified law was enacted not in France but in Bavaria, in 1756, and a similar project which started in that year in Austria resulted in the Austrian General Civil Code of 1811. This incorporated rules on a basic form of company, the *Gesellschaft bürgerlichen Rechts* which, although not offering limited liability, did give members the right to an annual financial statement. Another comprehensive codification which predated the French code took place in Prussia, but the *Allgemeines Landrecht für die Preussischen Staaten* of 1794 contrasted strongly with the egalitarian codified law of France. In the Prussian law, the individual’s legal position was within various communities, as a member of a given class, as a member of a family or household and as a member of an association or company. In this latter context, the law contained accounting regulations, but not with respect to the corporate form introduced in the French commercial code.

At a time when small independent European states were being drawn together into larger political units, the appeal of unified law was obvious. At the same time, in countries such as England where there appeared to be no such need to unify the law through codification, as its development through the common law was itself a form of centralisation, reformers such as Bentham were to appeal to another feature of codified law, arguing that the English common law was based on historical accident rather than rational design. But, if only to secure their monopoly by keeping the law obscure, English lawyers blocked the attempt to rationalise English law. Moreover, the threat of involuntary importation faded when Napoleon was defeated.

At its very outset, therefore, the regulation of accounting was the result of two countervailing factors, one reinforcing segmentation and the other facilitating integration. The first of these was the need to create a body of rules in each jurisdiction to govern business activity, which occurred in legal systems as independent as those of Prussia, France and England. The second was the rapid spread of the requirements laid down in the French commercial code which found their way within a matter of years into the law of numerous countries.

EUROPEAN NATIONALISM AND THE LAW

In the wake of Napoleon, the division of Europe under the Vienna accord of 1815 resulted in various manifestations of national unity. The Belgian provinces, which had earlier passed from Austria to France, rebelled against the enforced union with Holland and eventually gained their independence in 1830. Elsewhere, cultural renaissance in Greece led to independence from the Turks in 1829. At the same time, resistance to Austrian rule in Northern Italy led to Mazzini's *Giovine Italia* movement, the beginnings of a unified Italy. In contrast, certain other nations saw their influence diminish during this period. For instance, in 1814, in the wake of its alliance with France, Denmark was forced to cede Norway and, during the 1820s, Portugal and Spain lost their dominions in South America. This also led to a renewed focus on national concerns.

As mentioned earlier, the *Code de Commerce* came into force automatically in the Belgian provinces whilst they were under French rule and the commercial code remained in force during the short-lived union with Holland from 1815 to 1830. In Belgium, following independence, the new constitution contained the provision that the law be fundamentally revised '*dans le plus court délai possible*'. In fact, the delay was rather longer than expected and, with regard to company law, it was not until 1841 that a ministerial order specified the new regulatory powers. In the Netherlands, however, in spite of the country's independent legal history, the legislative framework did not revert to its original form following the split with Belgium. Instead, work started on a revision of the law which eventually unified the civil and commercial codes and was enacted in 1838.

In northern Italy, where codified law had entered with Napoleon's armies, French law was repealed in 1814. Nevertheless, the new laws that then developed in the various Italian regions were greatly influenced by this experience. In Spain, commercial law was codified in 1829 following the French model and, in Portugal, commercial law was codified in 1833 on the basis of the private work of Ferreira Borges who also relied on French law. In Greece, plans for codified law were made at the time of independence, when the spirit of the French revolution lent support to the notion of a civil code. However, in Greece, Roman law statutes of the fourteenth century were to form the basis of law. Indeed, the legal evolution in Greece was greatly influenced by German jurists from 1835 onwards when a German came to the Greek throne.

It was during this time that Prussia began to emerge as a focus of alternative nationalist hopes amongst the fragmented German-speaking peoples who, in 1815, had seen the creation of the German Confederation of 39 states, albeit under permanent Austrian presidency. In this politically fragmented Germany, debates about the desirability of a uniform civil code were bound up with the political question of German unification. Indeed, proposals to implement a French model of codified law did not succeed, but this was not only because of the political rivalries between the German states but also because of the clever manipulation of popular sentiment at a time when French expansionism had just been halted. An eminent German jurist, Friedrich Carl von Savigny, espoused the legal theory of *Volksgeist* – the spirit (*Geist*) of the people (*Volk*) – in which law is intimately bound up with the history of a wider society and grounded in the consciousness of its citizens (Savigny 1814).

Law, as the expression of *Volksgeist*, was portrayed as an organic growth like language. Savigny claimed that, as the modern German states had evolved from the Holy Roman Empire and, accordingly, had absorbed Roman Law over many centuries, the true law of the German-speaking people was embedded in their Roman law history. But Savigny's argument that law is the product of the 'spirit of the people' is not dissimilar to Rousseau's theory that legitimate government rests on the 'will of the people' in a social contract. In terms of the influential German philosopher, Immanuel Kant, the role of government would be that of serving the interests of free, equal and self-determining individuals. To Savigny, therefore, the new German legislation would be derived from Roman law and also interpreted in the light of Kantian ideals of individual autonomy. The notion of individual autonomy guaranteed by a formal body of rules equally applied to all led inevitably to notions of *Rechtsstaat*, and the political objective of unifying the German-speaking peoples to the *Allgemeines Deutsches Recht* (Ewald 1995).

Thus, the reaction to the French revolution by a German jurist led ultimately to a major divide in European law-making. It may even be argued that the principal schism in Europe was not that which is said to exist between common law and codified law, but between the tendency to imperial rationalism which placed the state above the law and the tendency towards social democracy which maintained the state within the law. After all, Savigny's theory of law was grounded in the *Volk*, implying that the ultimate source of legal authority lay with the people themselves. Indeed, for Savigny, it was essential that the law be developed not by judges but by legal scholars who would interpret the social context within which principles of law may be established.

The legacy of the Napoleonic era and the effect of Savigny's rebuttal of the abstract system of rules contained in the French code was to redirect the process of law-making in the emerging German nation, and other European countries where he was influential, to one of gradual unification of laws within their own national context. Indeed, to justify their own separate existence in the face of internationally unifying forces, national laws contained their own seemingly irreducible differences. Even in the area of company law, we can see the immediate effect in the differences between nations in the introduction of alternative forms of limited liability, variation in disclosure requirements and divergent approaches to shareholder and creditor protection.

THE EMERGENCE OF NATIONAL ACCOUNTING REGULATIONS

During the first half of the nineteenth century, successive attempts to unify the commercial law of the German states resulted in failure (Schlesinger 1988). But Roman law norms were decisive in bringing notions of periodic income (*fructus*) and the maintenance of the asset base into those laws which did emerge (Schneider 1995). Already, the Prussian law of 1794 contained its own rules for asset valuation, systematic depreciation and the distribution of profits, applicable in those cases where contracts did not specify otherwise. In an amendment to the Prussian Stock Corporation Law of 1843, the *Aktienrechtsnovelle* of 1856 stipulated income measurement in terms of net asset changes rather than revenues less expenses, and required that a company's paid-up net capital must be maintained in order to protect creditors. Commercial law in the German states was eventually unified in the *Allgemeines Deutsches Handelsgesetzbuch* of 1861 which was gradually adopted by all members of the Deutsche Bund. The political union of the northern German states took place in 1867 and the complete unification of the Deutsche Reich under Bismarck followed in 1871. The German commercial code required all assets and liabilities to be stated at their 'attributable value' (*beizulegender Wert*), which was interpretable as the current value at the balance sheet date (Ballwieser 1995). Subsequently, the first German *Aktiengesetz* in 1870 was explicit in allowing securities to be valued at market, but left many other accounting matters to be decided in the company statutes. However, following a number of instances where profits were found to have been overstated and improperly distributed, a revision of the *Aktiengesetz* in 1884 introduced an obligatory valuation system based only on historical cost, requiring asset depreciation and providing for capital maintenance by way of mandatory capital reserves. There was also now an obligation to publish accounts, supported by sanctions, but audits remained optional.

In Britain, the Joint Stock Companies Act of 1844 made it possible for the first time to incorporate a company by registration (although liability was still unlimited) and this law also required the annual presentation of a 'full and fair' audited balance sheet to the shareholders and its deposit with the Registrar of Companies. Limited liability for registered companies was introduced at the later date of 1855. However, in the following year, 1856, the compulsory accounting and auditing requirements were abandoned and replaced by optional clauses in company articles, including a standardised balance sheet (Napier 1995).

In France, when the *Société à Responsabilité Limitée* was introduced in 1863, the enabling legislation specified for the first time the role of the *commissaire* whose function was to report to a company's general meeting on the situation of the company and its balance sheet but who was not required to be independent of the shareholders or management. Four years later, the SARL was abandoned, but the advantage of incorporation without government authorisation was extended to the *Société Anonyme* in an Act of 1867, along with the obligation to publish a commissaire's report and accounts (Mikol 1995).

In Belgium, the first company law was enacted in 1873. Inspired by recent legislation in France, the Belgian law empowered *commissaires* chosen from shareholders or directors to monitor and audit company affairs and required the communication of a balance sheet and profit and loss account to shareholders (de Rongé, Henrion and Vael 1995). In the Netherlands, on the other hand, proposed legislation mandating financial disclosure was less successful as attempts to draft new law in 1871 (the Jolles Committee) and 1890 (the Kist Committee) did not reach the statute book (Camfferman 1995). In Denmark also, financial reporting remained unregulated, in this case because there were no such requirements in the 1862 *Firmaloven* nor in the 1889 revision which was intended to harmonise Danish commercial law with that of other Scandinavian countries (Christiansen 1995).

In Italy, not long after political unification in 1861, the *Codice Civile* unified the law of Italy and the *Codice Commerciale* followed in 1882. Committed to a liberal philosophy at the time, the legislature did not feel it appropriate to prescribe minimum disclosure or asset valuation rules, although the balance sheet was expected to show the 'true' profits and equity. Reliance was placed on shareholder representatives, *sindaci*, to exercise responsibility for monitoring the accounts (Took 1995). In Spain, commercial law was updated in 1885 (Inchausti 1995). In Portugal, the first company law was replaced in 1888 by a version which took account of the recent commercial codes of Spain and Italy (Ferreira 1994).

During the nineteenth century, new laws on company accounting migrated readily across Europe. In some cases, the importation was not voluntary (Belgium, the Netherlands and Italy). Some legal transplants were successful (Spain and Portugal) and others were rejected (Italy and Belgium). Harmonisation programmes were entertained in order to unify law (the German Confederation and Scandinavia), whilst others remained resolutely insular (Britain). Developments such as publicity and disclosure, creditor protection and capital maintenance, audit and supervision occurred throughout the continent, and the influence on law-making of new laws in neighbouring countries was readily recognised. However, the evolution of accounting law did not follow a straightforward pattern of development, as the search for national distinctiveness seemed ever to be present, giving rise to independent auditors in one country and shareholder supervisors in another, to strict adherence to historical cost in some jurisdictions and marking to market elsewhere, to compulsory disclosure in the more regulated economies in contrast to optional financial reporting in others. Thus, the effect of *Volksgeist* was to see a century which began with the harmonising effects of the French commercial code end with territorial claims over accounting regulation.

This distinctiveness in national accounting regulation has continued for much of the twentieth century, even in the face of the influence of universal phenomena such as hyperinflation and the growth of corporate activity. Of particular importance in this context is the case of asset valuation. Throughout the twentieth century, the development of regulations in this area of accounting has been as paradoxical as the earlier legislation on basic aspects of accountability. On the one hand, accounting rules have been transplanted from one jurisdiction to another, not only once but repeatedly throughout the century. On the other hand, the present state of regulation governing asset valuation reveals that the differences from one country to another are as striking as ever. In the following section, we provide a more detailed discussion.

3. Explaining Differences in the Valuation of Assets

Throughout Europe, the stimulus for the development of alternatives to historical cost accounting has been the incidence of inflation itself, the cycle of regulatory activity relating to asset revaluation being attributed to the renewal of inflationary conditions (Mumford 1979). Indeed, it was the hyperinflation in Germany during the early part of the twentieth century that first gave rise to different approaches to asset valuation which were later taken up in various European jurisdictions, the early German accounting theorists being proponents not only of the use of current values (Schmidt 1921) but also of indexing based on either prices (Schmalenbach 1921) or the gold standard (Mahlberg 1923). The German experiments with indexation based on the gold standard influenced French accounting theorists, as evidenced by the work of Delavelle (1924) and Faure (1926), whereas Schmidt's theory of current value (*Tageswert*) accounting was to influence the work of a Dutch accountant (Limperg 1937) whose own approach led to a fuller theory of replacement value (*vervangingswaarde*) accounting.

In 1924, the German *Goldmarkbilanzgesetz* became the first piece of accounting legislation to be based on price-level indexing, in an attempt to 'stabilize' the balance sheet with respect to changes in the value of gold (Sweeney 1927). A similar regulatory approach was taken in France in 1930 when the *Direction des Impôts* authorized firms to revalue certain fixed assets on the basis of the relation between the paper franc and the gold franc. Italy introduced a form of price-level adjustment later still, in 1936. In the Netherlands, on the other hand, legislation did not prescribe a valuation method but nevertheless acknowledged the existence of alternatives in practice by requiring, in 1928, disclosure of the method used (Zeff et al. 1992). The only other contemporary legislation dealing with this issue occurred in Denmark where, in 1930, a quite different approach to accounting for the effects of changing prices was adopted. This was based on the regular assessment of the value of land and buildings for tax purposes, which started in the 1840s (Christiansen and Elling 1993). The Danish *Aktieselskabslov* of 1930 permitted the revaluation of fixed assets when a permanent increase in value had taken place, thus recognising the longstanding practice of using taxable values in the financial accounts.

By the 1930s, therefore, the foundations were laid for continued differentiation between the various methods used to account for changing prices. Competing theories of accounting and varying requirements in law had become established in different national contexts, a pattern which was to continue when concern over the effects of inflation returned to the scene.

GROWING DISHARMONY

Accounting for changing prices reemerged as an important issue in the late 1940s following the discontinuity of war and again in the 1970s when the international economic order changed as oil prices increased. With regard to its impact on accounting, each of the nations of Western Europe continued to respond in its own way to inflationary conditions.

In Germany, the aftermath of war led to the introduction of a new currency unit, and the *Deutsche Mark Eröffnungsbilanzgesetz* of 1949 required all balances to be restated in the new Deutsche Mark for both financial reporting and tax purposes (Most 1977). On this occasion, companies were able to restate their accounts using current values, but the German legislator returned immediately thereafter to historical cost as the upper limit. In 1975, in the light of renewed discussions brought about by the oil price increase, a technical committee of the German auditing profession's *Institut der Wirtschaftsprüfer* issued a recommendation on accounting for capital maintenance (IdW 1975), calling for companies to provide supplementary information in which reported income would be adjusted with respect to equity-financed assets (Coenenberg and Macharzina 1976). The opinion was influenced by a number of voluntary disclosures at the time, including companies such as Portland Zement, Siemens and Mannesmann. But the recommendation was not binding and no changes in legislation occurred.

In France, revaluation based on purchasing power accounting was actively promoted in the post-war years. A decree in 1945 and a law in 1948 gave companies the right to revalue on the basis of published indices, but a further law in 1959 eventually withdrew the right with effect from the end of 1962. Even so, some companies continued with the practice. Such *réévaluations libres* (free revaluations) were tolerated although they were in breach of the commercial code, and were usually applied by loss-making companies as the unrealised gain incurred a tax penalty (Scheid and Walton 1992). The official regulatory body, the *Conseil National de la Comptabilité*, became involved in 1974 when it disallowed the practice of offsetting losses against the revaluation reserve and called for Government action. The French Government reintroduced revaluation in 1976, again using a price-level adjustment approach, this time permitting some discretion in revaluing all fixed assets at the *valeur d'utilité*, i.e., 'the amount which any prudent manager of a business would be prepared to pay for an asset with regard to its usefulness to the business', up to the amount based on the published indices (Collins 1994).

Elsewhere, in Italy, Spain, Portugal and Greece, the impact of inflation on accounting was regulated by the national tax authorities using price-level adjustments to accounts. In Italy, price-level adjustment laws were enacted (DL 436 in 1946, DL 49 in 1948, Law 91 in 1949 and Law 74 in 1952), each law authorizing firms to revalue various categories of asset in accordance with official price indices. These were followed at a later date by two further price-level adjustment laws (Law 576 in 1975 and Law 72 in 1983). Similarly, in Spain, revaluation was permitted for various assets, again based on official price indices (Law 76 in 1961, Law 41 in 1964, Law 12 in 1973, Law 50 in 1977, Law 1 in 1979, Law 74 in 1980 and Law 9 in 1983). The first of these pieces of legislation in Spain was largely ineffective due to the fear of a possible tax liability, but widespread acceptance was achieved in 1964 when it was indicated that there would be no tax penalty for companies which complied (Gonzalo and Gallizo 1992). In Portugal, unlike Italy and Spain, revaluation was limited to tangible fixed assets only, again governed by specific legislation (Portaria 20258 in 1963, Laws 126 and 353-B in 1977, Laws 280 and 430 in 1978, Law 202 in 1979, Laws 24 and 219 in 1982, Law 195 in 1983, Laws 143 and 399-G in 1984, Law 278 in 1985, Law 118-/B in 1986 and Law No. 111 in 1988). Finally, fiscal considerations also formed the legal basis for revaluation in Greece in 1959 and again in 1982 (Law 1249).

In the Netherlands, in contrast to the above, the post-war years saw Limperg's system of replacement value accounting adopted by some of the larger Dutch companies, including Phillips from 1945 onwards (Brink 1992). In the following years, two working parties were set up by the Dutch employers' organisations to study financial reporting (the Rijkens Committee in 1954 and the Hamburger Committee in 1962). Each proposed the use of current cost valuation for those fixed assets which would be subject to replacement. However, when the Dutch Government appointed the Verdam Committee (1965) to make proposals for a revision of company law, the view that current cost accounting was preferable to historical cost accounting was not shared. As a result, Dutch law continued to be imprecise with respect to valuation, and the company laws of 1970 and 1976 required the minimum of disclosure regarding valuation. The law gave considerable discretion to companies, which were permitted to base financial statements on accounting principles which were 'acceptable in the economic and social context' (van Hoepen 1984).

In the UK, the first expression of interest was in two proposals put forward by the Institute of Chartered Accountants of England and Wales: 'Rising price levels in relation to accounts' (ICAEW 1949) and 'Accounting in relation to the purchasing power of money' (ICAEW 1952). Each proposal rejected a change to any form of current value accounting, whether based on replacement costs or inflation indexation, and recommended that historical cost should continue to be the basis of published accounts. Nevertheless, it was suggested that the excess of reported profits over inflation-adjusted profits should be accounted for by the appropriation of profits to reserves. Even though these early proposals had no immediate effect, they influenced subsequent regulatory developments in the UK, which favoured the purchasing power approach (Tweedie and Whittington 1984). The eventual view of the Accounting Standards Steering Committee in the UK that a price index system was preferable to replacement cost accounting, was first expressed in its discussion paper 'Inflation and Accounts' (ASSC 1971). This paper eventually formed the basis for the publication in 1973 of ED8, 'Accounting for changes in the purchasing power of money', an exposure draft in which purchasing power indexation was proposed. Just before the discussion period was due to expire, the British Government set up an independent committee of enquiry (the Sandilands Committee) which rejected the purchasing power approach in 1975 and recommended current cost accounting. The provisional standard based on ED8, which had already been issued, was short-lived and was eventually abandoned in 1975 in favour of the Sandilands proposals which had Government backing. However, instead of regulating the issue itself in the Companies Act, the British Government left the task to the accounting profession, to take the form of a new accounting standard. In 1976, the Inflation Accounting Steering Group issued ED 18, 'Current Cost Accounting'. This exposure draft was also rejected, this time by ICAEW members opposed to the compulsory character of current cost accounting. In response, the Accounting Standards Committee produced a new exposure draft in 1979 which required current cost accounts to be published as supplementary financial statements by large companies only. This exposure draft eventually formed the basis of the first detailed set of rules on accounting for current values, SSAP 16 'Current Cost Accounting', which appeared in 1980. However, this professional standard was eventually suspended in 1985, partly due to continued dissatisfaction amongst preparers of accounts and also because the focus of attention had now switched towards the European company law harmonisation programme.

National barriers to harmonisation

The approval in 1978 of the European Community's Fourth Directive had the effect of forcing national legislators to reconsider their position with respect to the valuation methods used in company financial reporting. In fact, Article 33 of the Directive authorized Member States to:

> 'permit or require companies (a) to use the replacement value method for tangible fixed assets with limited useful economic lives and for stocks; (b) to use other valuation methods which are designed to take account of inflation, for items shown in the annual accounts including capital and reserves; (c) to revalue tangible fixed assets and financial fixed assets.'

The Directive did not specify the method to be used to account for the effect of price increases, but delegated the definition of revaluation and its mode of application to each country. Thus, even in the face of a concerted effort to harmonise accounting, national legislators had ample opportunity to continue to differentiate their own regulations from those of others. A similar situation surrounded the

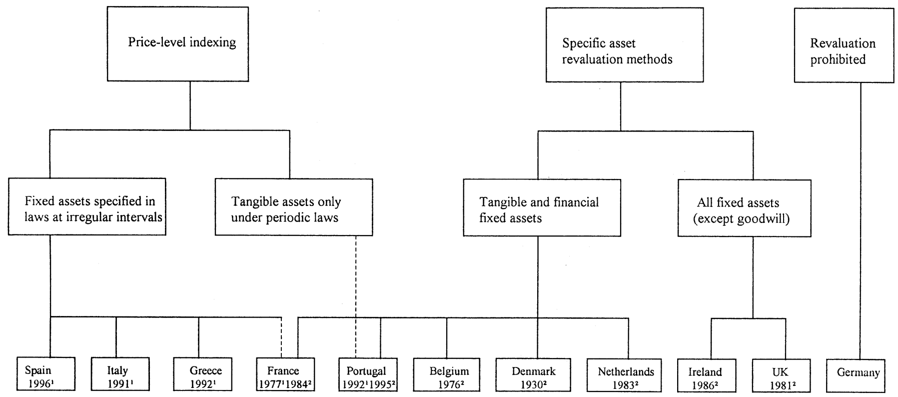

Figure 1. The current state of fixed asset revaluation in Europe.
Key: [1]indicates the year where the last fiscal revaluation law was enacted; [2]indicates the year where specific asset revaluation was first authorized by company law.

export through the Fourth Directive of the overriding British legal requirement of a ‘true and fair view’, with great linguistic variety emerging during the process of implementation and several countries changing the Directive’s original wording in order to accommodate national considerations (Nobes 1993). In the case of asset revaluation, the outcome for the majority of countries was that national law developed in a way which tended to reinforce the differences that already existed, with certain countries now legitimising the use of current values and others making price-level indexation obligatory (see Figure 1). The effect of the Fourth Directive on national regulations in the area of asset revaluation up to the present time is discussed below.

(i) Legal recognition of current values

Belgium, the first nation to base its company law on the provisions of the Fourth Directive, was also the first to opt in accordance with Article 33.1 (a) and (c) to legitimise accounting based on current values. In fact, as Belgium was in the process of replacing its largely obsolete accounting legislation, a law enacted in 1975 and an associated Decree issued in 1976 were able to take account of a preliminary draft of the Directive more than two years before its final approval. Although the Decree retained acquisition cost as the principal valuation rule, it also authorized companies to use replacement value (*valeur de remplacement*) for tangible assets as well as allowing for the revaluation of certain assets (Lefebvre 1984). The decision not to adopt a fuller version of inflation accounting was given in the executive report accompanying the Decree as follows:

> “In the absence of accepted opinion or tried and tested methods of inflation accounting (*comptabilité d’inflation*), the government does not intend to permit, still less enforce, their adoption before practical experience, particularly

abroad, makes a proper appreciation of the advantages, disadvantages and risks possible." (Lefebvre and Flower 1994, p. 100)

Belgian companies were only able to use replacement value for a few years as, having proved to be unacceptable for the purpose of determining taxable income and little used in practice, a further Decree removed the option to use replacement value in 1983 (Jorissen and Block 1995). However, companies still have the opportunity to revalue assets where the increase is certain and permanent, although no particular method has been specified.

In 1981, Denmark also allowed the revaluation of tangible and financial fixed assets without specifying the revaluation method in law, the revaluation of assets having anyway been allowed in Denmark since the 1930 Companies Act. Subsequently, in 1994, the notion of 'utility value' (*nytteværde*) was introduced with regard to the valuation of tangible assets in an exposure draft, ED11 (Christiansen and Hansen 1995).

The UK, by implementing the provisions of the Fourth Directive into the 1981 amended Companies Act, gave for the first time statutory support to current value accounting which had previously been a matter of professional standard only (Gordon and Gray 1994). The same occurred in Ireland when new company law was enacted in 1986 (Brennan, O'Brien and Pierce 1992). With respect to fixed assets, the British and Irish Acts permit the valuation of intangible fixed assets other than goodwill at current cost, tangible fixed assets either at market value or current cost and fixed investments at either market value or on a basis which appears to the directors to be appropriate. At that time, the accounting profession also took the step of stipulating that investment properties must be stated at their 'open market value'. In the meantime, an exposure draft on the revaluation of fixed assets (ASC 1990) recommended that, whilst land and buildings should be valued by external valuers, management should decide for every other class of asset whether to apply historical cost or a current value based on the open market value or, where an open market value cannot be determined, to use 'depreciated net replacement cost'.

The Netherlands also put current value accounting onto the legal statute when implementing the Fourth Directive, in 1983. In fact, even though replacement value accounting is traditionally assumed to have developed in the Netherlands, no reference to it existed in law until this date (Dijksma and Hoogendoorn 1993). The original intention of the legislator was to give preference under certain circumstances to current value accounting over historical cost accounting, but this was rejected by the Dutch parliament (Klaassen and Hekers 1995). The final legal provision (Art. 384) only allowed the application of current values to tangible and financial fixed assets and stocks. The definition of current value was included in a separate Administrative Order issued with legal authority by the Ministry of Justice. This distinguishes between three types of current value, namely (i) 'replacement value' (*vervangingswaarde*), which must be used if it is assumed that the asset will be replaced in due course, (ii) 'economic value' (*economische waarde*), which ought to be applied if replacement of the asset is unlikely and, finally, (iii) 'net realizable value' (*opbrengstwaarde*) which should be used only if the activity will not continue in the future.

(ii) Transition to current value accounting

In France, since the implementation of the Fourth Directive in 1984, the Commercial Code authorizes the revaluation of tangible and financial fixed assets on the basis of current value (Art. 12). The Government thereby legitimised the *réévaluations libres* which some companies carried out beyond the scope of the law. France therefore changed from price-level accounting, enacted in 1945 and 1959, to a form of current valuation with price-level indexation as the upper limit in 1976, to officially-sanctioned revaluation from 1984 onwards. However, French law does not specify the revaluation method. According to Griziaux (1995), revaluation is to be based on the concept of *valeur d'utilité* as applied on the occasion of the last legal revaluation in 1976, on which various parties have issued opinions.

In Portugal, the Fourth Directive was implemented in 1989, and integrated into the *Plano Oficial de Contabilidade*. The text of the POC requires the use of 'costs of acquisition or production, either in nominal or in constant escudos', suggesting that current purchasing power accounting would be legally acceptable, but not current cost accounting (Ferreira 1994). It should be recalled that, throughout the 1970s and 1980s, Portugal had issued general price-level adjustment laws at frequent intervals, and two more such pieces of legislation followed the implementation of the Fourth Directive (Law 49 in 1991 and Law 264 in 1992). At the same time, a number of Portuguese companies started to revalue assets beyond the levels authorized by these tax laws, particularly when book value was substantially lower than market value. This legal uncertainty with respect to revaluation has since been clarified as, in May 1995, the legislator issued *Directriz Contabilística* No. 16 in which the current valuation of tangible fixed assets is permitted, based on replacement value, market value or price indices.

(iii) The continued use of price-level adjustments

When Greece implemented the Fourth Directive in 1986, the legislator authorized the revaluation of assets but only in accordance with special revaluation laws. In fact, these still refer mainly to land and buildings (Papas 1993). Subsequently, such laws were enacted in 1988 (Executive Order 2665) and 1992 (Law 2065), the latter making the revaluation of land and buildings compulsory every 4 years.

The situation is similar in Spain where, after the implementation of the Fourth Directive in 1989, the legislator's position did not change with respect to asset revaluation, as the new accounting regulations and the amendments to the *Plan General de Contabilidad* indicate that a company may revalue only if there is authorisation under a special revaluation law (Díaz and Torre 1995). The latest such asset revaluation law was enacted in June 1996.

Italy, the last EU country to implement the Fourth Directive, saw further price-level adjustment laws (Law 408 in 1990 and Law 413 in 1991) in the months preceding implementation (Riccaboni and Ghirri 1994). Upon implementation of the Directive at the end of 1991, any opportunity for companies to revalue on their own account was removed by the *Codice Civile* which restricted revaluation to special revaluation laws from 1992 onwards.

(iv) Strict adherence to historical cost

In contrast to the above, Germany remained resolute in its support of historical cost accounting when the Fourth Directive was implemented in 1985 (Ordelheide and Pfaff 1994). This position had been made clear previously at the Council meeting at which the Fourth Directive was adopted in 1978, when the German delegation explained that

> "for reasons of monetary and economic policy, the Federal Government cannot accept valuation methods designed to take account of inflation as authorized by the Fourth Directive Art. 33 by way of derogation from the purchase price principle laid down in Art. 32. It will therefore not permit such valuation methods in the Federal Republic of Germany" (van Hulle and van der Tas 1995, p. 999).

4. Concluding Remarks

It has been argued in this paper that international diversity in the rules of accounting is partly a function of the desire to preserve local jurisdictions by maintaining national distinctiveness. Indeed, the early history of accounting regulation in Europe is bound up with the construction of the nation state and, in spite of the rapid spread of corporatism in the nineteenth century, the beginnings of governance took place in an environment of legal parochialism which led in turn to the emergence of different sets of regulations in the various nations of Europe.

Later, in the 1920s, when inflation accounting was legitimised in Germany and France, the new laws based on the gold standard were designed to meet another universal phenomenon, that of high inflation. Yet, in the fullness of time, this also led to regulatory solutions as diverse as the use of price-level adjustment methods, the recognition of current value and strict adherence to historical cost. In these circumstances, the implementation of the Fourth European Directive mainly reinforced the national distinctiveness which already existed. In Germany, for instance, revaluation was not considered in any form. In Greece, Spain, and Italy, revaluation was restricted to the existing method of price-level indexation. In the UK and the Netherlands, harmonisation resulted in statutory reference to current valuation approaches already in use in practice.

To some extent, this outcome may be associated with the subordination of asset revaluation regulations to company law in some jurisdictions and tax law in others, any change to the regulations being resisted on the grounds that new concepts might cause the particular legal system to lose its internal logic. Indeed, there has been a tendency to maintain the system of issuing periodic price-level adjustment laws in those jurisdictions where the rules of accounting are determined by fiscal considerations, whilst current value accounting has occurred where accounting has been governed by company law. However, there are some exceptions to this rule. In Belgium and France, where voluntary revaluation using current value is authorised, there is nevertheless a strong link between mandatory financial disclosure in published accounts and tax assessment. But it is also the case that, in Belgium, a special tax law exempts the surplus on revaluation from taxation whilst limiting the depreciation for tax purposes to acquisition cost, whereas the French fiscal authorities tax the revaluation surplus and permit companies to charge the increased depreciation on revalued assets against profits. Thus, it would seem that the law finds ways of dealing with the import of new concepts without prejudicing the coherence of the legal system. In this respect, the example of asset revaluation appears to negate the view that international differences may be explained simply by categorising national accounting 'systems' on the basis of certain characteristics of their business environment (e.g., Nobes and Parker 1995). On the contrary, we would argue that the balance between the factors influencing accounting regulation will vary through time and from country to country, and even from one accounting issue to another, and that the driving force of national distinctiveness is the ongoing struggle between the forces of globalisation and the pursuit of autonomy by individual states.

Thus, we return to the view that the events described in this paper are the result of an underlying process of competition and conflict between nations. When law is written to reflect 'the spirit of the people', national legislators seek to give their own legal rules a particular character. If laws were the same from one country to the next, separate national legislatures would be difficult to preserve. Whether the present differences in the laws of nations have arisen by design or by accident or as the product of unequal bargaining by those parties seeking to influence the law, they have nevertheless become institutionalised, giving national legal systems their own separate internal logic and coherence. Consequently, in the face of institutional intransigence, or sometimes for overtly nationalistic motives, territorial claims over accounting regulation persist. Indeed, the limited success of the European programme of legal harmonisation has given rise through the principle of subsidiarity to the mutual recognition between Member States of regulations which are not the same (van Hulle 1992), and it is notable that in introducing this principle the Maastricht Treaty of the European Union returned to a rhetoric not dissimilar from Savigny's *Volksgeist*, where policy decisions should be taken 'as closely as possible to the citizen'. Nationalism continues to cast its shadow over accounting regulation.

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