

REGULATION VERSUS THE MARKET FOR THE PRODUCTION OF ACCOUNTING INFORMATION: A REVIEW OF THE THEORY IN THE CONTEXT OF SUB-SAHARAN ECONOMIES

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Abstract: *This paper examines the plausibility of the arguments for and against regulating the production of accounting information. The literature is reviewed and discussed in the context of Sub-Saharan Africa countries. After a careful review of the debates and the contemporary theories of financial disclosures, it is argued that voluntary disclosure mechanisms cannot be used as policy instruments because of the absence of institutions. Two epilogues are provided: first a general one and the second specific to Sub-Saharan economies.*

1. INTRODUCTION

Background

Since the late seventies, research on the role of accounting information and its production methods has changed its traditional style. Research paradigms and design methods have changed particularly with the publication of Watts and Zimmerman's [109] seminal works on positive theory. The availability of methodological guidelines [6, 35], organized databases and powerful soft-wares facilitated the change. Though epistemological controversies (see [49] for reviews) continue, at least the norm has become examining ontological (reality) issues.

Empirical research in accounting has come up with some theories that attempt to explain and predict accounting practices. For instance, there is now substantial evidence which shows that firms disclose information voluntarily. Analytical research has also demonstrated that firms have a threshold level of discretionary disclosures [105]. Various stock market based research has documented that some price reactions can be observed because of mandatory accounting changes [65]. Cumulatively, from a policy point of view, these results in turn brought a more fundamental question: whether socially optimal level of accounting information can best be produced under

a regulatory environment or through the adoption of voluntary/ non-regulatory corporate disclosure mechanisms. These questions have important implications to countries which are in the process of selecting policy options and to those which are re-examining their past financial reporting policies.

Normative Versus Positive (Accounting) Research

Many accountants in the developing environments, as a result of their training orientation, are familiar to the concepts provided by what is now known as the true income school. In the sixties accounting terms like principles, assumptions, postulates, axioms and concepts started appearing in the literature. The ideas embodied in these terms have been presented (for example in textbooks) as the core theory of accounting standards. The school [73, 42, 86, 17] is now viewed as the school of accounting classics. However, the contributions of this school did not go beyond emphasising that accounting should have better measurement techniques. From a policy point of view, the effects of these early thinkers were the establishment and /or the strengthening of standard setting bodies world-wide².

The next school concentrated on studying the "usefulness" [1, 50, 51] or the "true and fair view" [3, 33] of financial statement numbers. However, as their predecessors, and because of policy biases of such research, most of the arguments had prescriptions in mind. They saw accounting as a technical problem involving mainly measurement issues. As a result, the debate as late as the early eighties focused on defining the "objectives" of accounting. Accounting faced philosophical and methodological problems. Sound theories and tests of theories were seldom found in the literature. Recognition of this situation obliged some researchers (see for example [68]) to be concerned with developing a "theory of" versus a "theory for" accounting. These weaknesses made accounting vulnerable to attacks from all corners [11, 13]. Criticisms continue, and more recently accounting is alleged to be "the problem" rather than part of the solution of control [73]. Collectively, most writings of this school were described as normative and rhetorical. Nowadays, the main stream journals abound in North American schools have more or less established a norm of their own: anything that is not testable and verifiable [89, 61] is regarded less scientific.

Our Place in the Research World

In the rest of the world, the academic accounting community can be classified into four main groups in relation to the new research direction: (a) The leftists: those who argue that positivism cannot be a leading criterion to the validation of accounting research [19, 64, 104]; (b) The social democrats: those who are trying to follow the new paradigm (mainly researches on European databases [92]); (c) The psychologists and the populists: those who see accounting as a "human science" to be studied in the context of organizations [47, 66]; and (d) The fourth group is mainly focusing on the so called Third World Accounting [94, 48].

With some support from the Britons, the latter group has now started to develop the equivalent of a dependencia theory for accounting³. The premises for the shift was the alleged inappropriateness of the type of accounting technology that is being transferred; presumably not epistemological⁴. Other than this, the literature on African accounting is scanty. It is not published in the "main stream" journals. The few that are available are confined to doctoral dissertations which are not commonly available to policy making institutions. The works that are available are mostly results of commissioned research. Such works are usually done by foreign experts, and funded by donor/multilateral institutions. The studies involve surveys and largely remain descriptive.

Objectives and Summary of the Research Problem

This paper has the objective of examining the plausibility of anti-regulation thoughts, in the context of the production of accounting information. The theory of corporate information disclosure is analysed in the context of Sub-Saharan economies. The paper attempts to review and discuss the theoretical basis for the regulation of the production of accounting information. Towards the end, country specific policy recommendations are made. The paper does not address the extent to which information markets should be regulated.

The paper is presented in the following order. In section II arguments for and against regulation are presented and discussed. In section III, observations on the plausibility of the arguments are dwelt upon and the competing contemporary theories of corporate disclosure presented. Section IV depicts the Sub-Saharan situations and introduces accounting in the context of development

and institutions. It analyses the relevance and implications of the theories to Sub-Saharan economies. Section V presents the conclusion and direction(s) for future research.

2. PRO AND CONTRA REGULATION ARGUMENTS

Ever since regulatory bodies like the Securities and Exchange Commission (USA) were created, there has been reservation as to whether regulating the production of accounting information is socially useful. Several questions such as the following have been raised. What are the merits and who are the beneficiaries of regulation? Is it true that unregulated markets are better in achieving optimal resource allocation? How does one characterize accounting information: as a private good or a public good? These questions continue to be asked today. However, the answers to these and other similar questions largely depend on who one asks: those who are for or those who are against regulation. Further, the analytical models used to find answers to these questions are largely drawn from general equilibrium type models and centre on information economics [46, 24].

Regulation Free Thoughts

These arguments are based on the premise that firms have incentives to report about themselves to an extent that no external rule governing financial reporting is necessary to produce the financial information needed for the efficient functioning of the economy. Agency theory, efficient market hypothesis, the private acquisitions of information that is not voluntarily reported are the main arguments presented in support of unregulated accounting information (markets).

Agency Theory

Many of today's business concerns can be best described by this theory [55]. The recent version of the theory tries to explain organizational behaviour in the event of the breakdown of Fisher's separation theorem⁵.

The conflict of interest between agents and principals necessitates nontrivial monitoring costs. These costs are incurred mainly to force (or entice) the agent to behave in line with the dominant

principals. Monitoring costs however, reduce both the value of the firm and the agent's compensation. Hence, it is argued that the agents have an incentive to minimize agency costs by reducing their conflicts with owners. Accounting based executive compensation schemes, budgets, audits and even the market based ones (for instance stock options) are devices used to reduce agency costs.

In this regard, corroboration of the theory shows that even the early English firms (the merchant guilds) voluntarily kept accounts that were routinely audited by the owners; long before mandatory rules were made (in the thirteenth century)⁶. Agency theory therefore, suggests that managers have an interest in reporting voluntarily and reliably, making mandatory disclosure rules unnecessary.

Competitive Capital Markets

This argument states that firms have an incentive to report voluntarily to the capital markets even in the absence of mandatory disclosure requirements. The competition among firms for scarce risk capital obliges the firm to inform the market about itself. The theory further states that firms which report more extensively and reliably would be able to raise capital easier and cheaper [98, 18, 60]. The empirical support for this hypothesis is largely drawn from the efficient markets theory. Most of these "event studies" followed positively normative methods (computations of cumulative excess returns) to test the Fama-Jensen version [28, 54] of semi strong hypothesis. A number of researches (see [92] for reviews) have reported that there is some evidence which shows the movement of systematic risk coefficients (betas) around the announcement of disclosure standards. That is, disclosing firms had lower betas than non-disclosing firms⁷.

These reports suggest that all companies which have good performance would have strong incentives to report fully and reliably. Those who do not report, could still be better off by reporting even "bad" information in order not to lose credibility from the stock market. Such an arrangement, it is argued, does not require the prescription of external disclosure rules.

Contractual Opportunities

Wolk et al. [115] note that any information not voluntarily reported under deregulation, can be obtained for a price by privately contracting with the firm itself, its owners or the information intermediaries (example: financial analysts). The market will determine how much information should be produced and the price. This arrangement can lead to a more efficient allocation of resources to information production. Subscriptions to investor newsletters and fees for investment advisors are examples that people are willing to buy the information that they think is useful. Under such an arrangement, regulatory intervention is not only unnecessary but also undesirable since the market itself determines the optimal quantity of information and its price. Accounting information here is treated like any other normal good, where quantities and prices are determined by demand and supply forces. In short, the price system solves the problem.

General Scepticism Against Regulatory Bodies

The widely held view is that regulations are corrective measures for market failures. However, here too there are competing and differing views about the beneficiaries and benefits of regulations.

Conventional wisdom of regulations is that society at large benefits from such rules. Particular emphasis is given to investors with small holdings who are unlikely to be well represented in the board of directors.

The second view states that regulations do not benefit anybody. There are no clearly identifiable groups which are gaining. The social benefits that may be obtained by regulating an activity or a market are taken up (eaten) by the implementation costs. Thus, the net benefits of regulation at the aggregate level are negligible.

The third argument is basically a corroboration to the second. It states that regulations benefit policy executing bodies themselves. Regulatory bodies established to deal with a particular problem stay long after their alleged purpose is no longer relevant. In short, it is argued that policy implementing bodies and their bureaucrats maximize their stay and get the benefits that may come out of the regulation.

Pro Regulation Thoughts

In the foregoing section we have seen four main reasons for unregulated information markets. The protagonists of regulation also provide several arguments. They are: (i) the firm is a monopolistic supplier of information; (ii) information asymmetry problem; (iii) the public good character of accounting information; (iv) externality problems under unregulated information markets; (v) the speculation problem; and (vi) the aggregate social consequences (public policy aspects) of unregulated markets. These points are collectively referred to as market failure arguments.

The Firm as the Sole Producer of Information

One of the causes of market failure is that the firm is a monopolistic supplier of information about itself. In an unregulated market, the firm can restrict the production of information and charge monopoly prices. This results in inefficient allocation of resources. Mandatory disclosures would result in more information and a lower cost to society (*ceteris paribus*) than could be achieved in unregulated monopolistic information markets. Hakansson [97] suggests that the production costs of mandatory reporting requirements may be small since most of the basic information is produced as a by-product of internal accounting systems. If this is the case, then the social costs of mandatory reporting may be small, making such reporting more efficient than the private buying of information. Moreover, searches by information intermediaries about firms could be resisted for another reason. Privacy concerns (breaking the law which provides for the right to privacy) can be a major hindrance to making such options operational. This makes the plausibility of anti-regulation arguments weaker.

The Asymmetry Problem

Even under regulation, accounting and auditing have been criticised for low quality reporting (Briloff *op cit*). Fraud not detected by auditors and the absence of "truth and fairness" in the numbers contained in annual reports require regulatory agencies to protect public interest. The so-called creative accounting is a case in point. Another typical case which shows that annual reports do not mean much is that of the Dutch conglomerate Phillips N.V. In May 1990 its stock price collapsed, the firm engaged in heavy restructuring. Nevertheless, the annual report for the (preceding) year did not signal any of these events.

Information asymmetry occurs when one individual is endowed with more information than the other party (for instance in a transaction). In a seminal work, Akerlof [2] demonstrated how difficult it is to distinguish "the lemon" products from the good ones. In other words, there is an adverse selection problem. In the market for information, information asymmetry about securities can lead to a situation where "good" and "bad" securities (securities with different returns and same risks or vice versa) can be traded at the same price. One of the major lessons of market efficiency that advises investors to trust market prices ([10 p.272] for example) faces a breakdown. The market becomes inefficient (in the Beaver op.cit sense) in processing information and prices may not indicate the real worth (intrinsic value) of the security. Godenes et al [41] noted that Akerlof's (op.cit) analysis of quality and price can be extended to the accounting setting. Therefore, more and better regulations are necessary; not only to improve disclosures but to curb the activities of those with more information from reaping the benefits that result from their privileged access to organizational information.

The Speculation Problem

The speculation problem is created by market participants (investors, information intermediaries, etc.). Heterogeneous beliefs and imperfections in capital markets create grounds for speculations about the firm; for example before the publications of annual reports or the announcement of earnings. Transaction costs are incurred (in security trading); the market place is busy and prices are altered. This is happening not because something underlying the firm's investment/asset structure has changed, but purely on speculative grounds. The search for information continues at an extensive level for the validation of rumours. This situation obviously does not change aggregate real wealth in the market but the firm's market value changes simply because of speculation motives. Here, the speculation creates wealth transfers (as in gambling) and does not increase the pie. Therefore, it is argued that regulatory disclosure helps in curbing such undesirable behaviour of market participants. Laws that require the disclosure of "material information" that affect value and/or penalties for fabricating rumours are intended to curb such activities.

The Externality Problem

If the market for information is left unregulated, the result will be competition among firms in reporting information about themselves. Firms who are caught in this competition may be forced to release strategic and sensitive information simply to overcome the market's wrong pricing of their securities, if they do not disclose. Absence of information can be interpreted as bad news. Taken as a whole, the disclosure practices of one firm influences the other firms' disclosure policies. The type of externality could be both negative and positive. First, it enhances disclosures and thus, corporate transparency. Secondly, on the negative side, the practice can push some firms into a disadvantageous position⁸. Therefore, it is unlikely or rather difficult to assume that firms by themselves will internalize such costs [34]. Accordingly, regulation is not only desirable but also necessary.

The Exclusion Problem

Accounting information can be characterised as both a public good [67] and a private one [102]. Information can have a private value if its arrival is ex-ante to a decision and that information is held privately. Ex-post public information has only social values [46 op cit] and no private value.

Public information (for example annual reports) can be freely passed from person to person and the consumption by one does not exclude the consumption of the same information by others; once annual reports are issued⁹. This brings financial information, specially those released through annual reports closer to a public good. Public goods are underproduced in unregulated markets because consumers under-reveal their preferences. Thus, "free riders" benefit from the good or the service not only without paying but by not even admitting that they need it. And a public good producer who attempts to exclude non-payers incurs non-trivial costs. Therefore, anti-regulation arguments are further weakened.

Moral Hazard and Epistemological Problems

Regulations are usually considered as correcting tools for market failures. In other words, economic regulations are aimed at curbing the under/over production of a public or private

commodity. In addition to the above market failure arguments, the moral and redistributive issues resulting from non-regulatory practices become reasons to intervene in the process of "well functioning markets". In other words, politicians may not like the distributional impacts of such markets. Helleiner [45, p.542] for example notes the following:

... almost imperceptibly, prisoners of their own paradigm, students of economics risk in beginning to regard all government policies as interventions; likely to impede the harmonious functions of the market and beginning to regard distributions of income and power as a matter wholly independent of market functions to be handled by separate policies (lump sum transfers) that do not interfere with markets...

Self interest [44] and unregulated market theories also face epistemological issues. Christenson (op cit), Low et al (op cit), Tinker et al (op cit) argue that self interest and regulation free arguments take market phenomena as natural and universal. The supporters of regulation-free information markets ignore the institutional backgrounds that define the rule according to which market behaviour is played out. In short, they are value-laden. Therefore, it is argued that the advocates of anti-regulation in fact justify a particular type of social contract.

3. GENERAL EPILOGUE AND A COMMENT ON THE CONTEMPORARY THEORY

Given both sides of the debate, it is now proper to make some observations and examine the current theories of disclosure. In the first section, we report our earlier observations [53].

- a. Since managers have incentives to reduce agency costs, there would be substantial disclosure without mandatory disclosure rules. The contractual terms that define the relations between the agent and the owners would normally make provisions for trade-offs between full monitoring costs and the level of incentives to induce the manager to have an interest which is in line with the owner.
- b. Regulated financial reporting causes or facilitates a transfer of wealth from the firm or its customers or both to the users of financial information. How much wealth is transferred depends on the extent to which the firm is able to pass the costs of regulation compliance

- to its customers through higher product prices. Nevertheless, it is obvious that the firm's information system is part of the technology applied by the company in making its products available to the market place.
- c. Standardization of accounting policies and procedures (semi-regulated information) leads to more uniformity among companies than would occur in unregulated markets. This improves the comparability of financial statements; including those prepared across national boundaries.
- d. Research in the seventies and eighties concentrated on finding the microeconomic consequences of increased corporate disclosures. Most researchers examined the behaviour of security prices and risk coefficients around the promulgation of new mandatory (accounting) disclosures. The evidence by and large is that those firms that complied to the new standard or those firms which have been disclosing voluntarily selected items of information were characterised by lower systematic risk and returns [92, 21, 25]. Despite the ample reports, some (see for instance [15]) suggest that reporting patterns do not describe any economic phenomena.
- e. Between these extremes one finds Verrecchia's [105] proprietary cost theorem. Using analytical methods, he shows that because of the existence of (constant) proprietary costs (which may be endogenous or exogenously determined), a firm will have "a threshold level" of discretionary disclosure. Thus, the existence of proprietary costs mitigates the adverse selection problem; in favour of full disclosure. This argument looks plausible particularly if the firm has good news¹⁰.
- f. Darrough and Stoughton (op cit) and Verrecchia [106] further show that firms not only disclose voluntarily favourable news but even bad news. The purpose here is deterrence of (potential) competitors' entry to product markets. In a more recent work, Skinner [99] provides evidence which shows that managers disclose bad news promptly and states that they behave as if they are facing "asymmetric loss functions" in choosing their voluntary disclosure policies. In other words, managers behave as if they bear large costs when investors are surprised by large negative earning news. Skinner's explanations are stockholders' ability to sue and the incidence of reputation related costs (for managers).

In short, managers have both legal and reputation (market) incentives and attempt to preempt large negative earnings surprises. Skinner's findings are not claimed to be proprietary cost variables.

4. IMPLICATIONS OF THE DÉBATES TO SUB-SAHARAN ECONOMIES

A Profile of the Sub-Saharan Situations

Most Sub-Saharan countries are roughly three decades old as nation states. Slave trade, colonialism, commodity production, independence resistance characterized their recent history. Post-colonial states spent a considerable time in "nation building" exercises. In the process, massive attempts of the centralization of the economy and the administrative structures followed. The contradictions between colonial influences (institutions) and nationalism became serious. The cold war exacerbated internalized contradictions and Sub-Saharan Africa became the battle ground of the East and the West. The proxy wars and latent internal conflicts ruined the fabrics of society and institutions (new and old). As a result, many states have collapsed (Somalia, Rwanda, Burundi) or are nominally existing. Now, pluralistic models are being tried without fundamental institutions. Trust and credibility of the modern political institutions and the legal systems are disappearing. Enforcement of basic laws and contracts is curtailed by capacitation problems and frequent political interventions. Information is obtained through personal, tribal, religious and (to some extent) trade networks. Under such a scenario it is no surprise to find that there is little public interest in published (accounting) reports.

Macroeconomic indicators show consistent and long-term economic regress [97]. Transitions to "market oriented economies" are being pursued as a panacea in nearly all the states. And the prescriptions of the Brettonwood institutions are fairly standard (see [52] for example). Dismantling command economies, rearrangement of property rights, trade liberalizations, macroeconomic stabilization, currency realignment programmes, reducing budgetary deficits are vigorously pursued. Yet, these shocks are not responding "as expected". Lessons are being learned by doing. Clear choice on the speed (gradual versus rapid) of liberalizations of the formal economy [69] has become controversial. Moreover, the limits of financial reform programmes

[26, 39] are overlooked. As a result, in most countries of the region, there is a serious problem of macroeconomic control. Further, reliance on the command and control institutions of the reform programmes has become dubious. This worsens the process of trust making in largely traditional and pre-capitalist societies [88].

The search for the "invisible hand" has become difficult to identify in these societies. Some times one sees it, and other times one does not. Despite this, some monetarists perceive the problem as if market (concepts, mechanics, paradigms, policies and rules) can be implanted in the absence of organized (market) institutions.

The indigenous institutional settings consist of an interdependent web of organizations most of which are not characterized by increasing returns. Trust making and uncertainty reduction largely rely on tribal, religious and personal affiliations [93, 80] than on published reports and records. As a result, transaction cost, information asymmetry and cost of information search are deemed high in these societies.

In the "informal" sector, petty traders compete intensely by having a bazaar type (Suqe) trade. Peasant agriculture remains the main-stay of the economy in most of the countries. Governments' influence and controls in these sectors are minimal and mostly rhetoric. Economic historians (see North op cit for example) provide evidence that such institutions did not evolve to advanced (economic) organizations.

In the formal or upper strata of the economy, one observes some multinational companies, some "home-grown" entrepreneurs and state owned enterprises (SOEs). Most of them are import substituting concerns. The multinationals use their subsidiaries for vertical integration; mainly for obtaining raw materials and commodities or for developing non-overlapping geographical markets. The SOEs sector is in the process of restructuring. That involves property rights rearrangements. For a number of reasons the SOEs sector has become prone to dismal financial performance [78, 103, 76]. In the finance sector, the commercial banks still serve their precolonial time purposes; mostly the facilitation of commodity trade [80]. Credit rationing is high. Secondary markets are few and small. The tradition of "la bourse de papa" is nonexistent. Where secondary markets exist, they are characterised by price distortions, thinness, volatility, liquidity problems, lengthy settlement procedures and under-capitalization. Most of the shares

are held by institutional investors.

Development, Markets and Accounting

With the above ontological factors, then comes the thorny issue of development¹¹. Various paths have been suggested to the study of African development. They include environment, population (demography), institutions (state and law) and price theory. The literature on price theory overshadows the others. The result is that many observers have concluded on shortages of capital and trained manpower as the crucial seeds for closing the gap between Sub-Saharan countries and MDCs.

These perceptions of the problems and the resultant solutions are not free of puzzles however. If the price system and market rule were making more sense in these economies, one would guess that shortages (capital and trained labour) would be reflected in prices. That is, the marginal rates of returns on invested capital and wage rates of the trained should have been higher in the region (compared to MDCs). What we see is rather capital flight, trained labour "exodus", etc. The relation between price and scarcity is indeed basic to price theory.

These facts signal that rather than searching answers to the problems of underdevelopment in the area of price theory, a closer look at Alfred Chadler's (1977) "visible hand" (see also [87, Porter 1990]) perhaps provides a better insight.

An economy is as strong as its institutions [37]. Arrow [3, p.33] also notes that: "organizations are a means of achieving the benefits of collective actions in situations in which the price system fails". Institutional economics [20, 114, North op cit] despite its limitations [32], focusing on institutional evolutions may offer a better venue than reliance solely on general equilibrium theory. Stiglize[100, p.202] for instance notes the following:-

...Indeed, the difference between MDCs and LDCs lies largely in matters of economic organization... then the first item on the research agenda should be a better understanding of the microeconomies of LDCs...

Still another issue is whether "the market" system in itself is or can be self regulatory in this environment¹⁷. Platteau [88] stresses the need to posit fundamental institutions or constitutional rules that contain agent's behaviour in order to bring coherence to the market system. Platteau [88] goes further and argues that whatever analytical path one follows, the problems of institutions or social norms cannot be evaded (P. 545). Institutions and social norms' major role in a society are to reduce uncertainty by establishing a stable (but not necessarily efficient) structure of human interaction.

Hence, the development process must then concentrate on one hand the building of new institutions and on the other hand, understanding ways of facilitating changes into existing institutions. Evidently, both old and new institutions ought to be characterized by increasing returns. Additionally, keeping aside the intuition that markets are self regulatory, even by its own standards of market failures, the need for a supra individual mechanism that facilitates trust, coordinate efforts and enforce agreements is basic.

Accounting's role becomes much larger when discussed in the light of real institutions (closed and open systems) rather than in the context of abstract price theories. If this is the case, the main challenge is whether there could be an extrapolation from some aspects of institutional economics [20, 80], organisations [96] and accounting [8, 109, 59]. A multi-disciplinary matrix is required to develop a theory for less "rationalized" economies. In other words, "rediscovering" Sub-Saharan institutions is basic to the understanding of the problem. The objectives of such a marriage should be: widening and deepening the market, establishing trust, facilitating institutional evolutions, reduction of transaction costs and information imperfections, transformation of uncertainty into risk. In short, mitigating the extent of market failures and identifying the areas where the supra individual institutions' involvement becomes optimal. As Platteau [88] notes, stable orders can be produced in the market place and the problem of trust making can be mitigated only by assuming the existence of rules (with enforcement capacity) that constrain behaviour. *Ceteris paribus*, the need for a supra institution, the next formidable question is knowing how effective such an institution can be in restoring trust.

Epilogue Two

If the foregoing is a fair presentation of competing theories and the prevailing situations in Sub-Saharan countries, then, we should be able to examine where the current accounting debate stands. We should attempt to answer the plausibility of anti-regulation arguments in the context of Sub-Saharan economies. First, for the reasons explained in previous sections, competitive capital markets fall short of describing the ontological aspects of these markets.

Agency theory, however has the potential to describe some institutions in the upper sector of the economy. Nevertheless, the idea that a typical indigenous African firm can be described as "a nexus of contracts" remains abstract as most firms are not share companies. More importantly, agency theory has the potential to explain the SOE sector. Here, there are at least four stages of agencies: the public shareholder but without shares, the parliament, the government and the manager of an SOE. Thus, the monitoring mechanism for the owner becomes complicated and expensive. Nevertheless, the multiple stages do not rule out some level of (voluntary) disclosures.

On the pro-regulation side, nearly all arguments hold for Sub-Saharan economies. Again, mostly for the upper strata of the economy. The asymmetry issue however, needs a closer look.

The asymmetry problem is less serious in the village economy, even by the standards of Akerlof's [2] lemons principle. Sub-Saharan village and nomadic societies do not commonly charge interest on borrowed money. The economy is less affected by monetary (interest rate) policies and borrowings are restricted within families and distant relatives circles. The punitive consequences of dishonesty are more than its financial benefits.

The concept of interest and hedging against default perhaps are implied in lendings granted by proto farmers: where the borrower in return is required to work in the fields. In short, the Indian village money-lender traditions are not predominant and Islam has a role.

The asymmetry problem becomes suddenly visible in traditional bazaar type markets (Merkato of Addis Abeba, Mbare of Harare for example); where trust and honesty in trade are established after several contacts. The problem becomes complicated if trust is established through intimacy,

especially in environments where certain ethnic or religious groups specialize in (petty) trading. Hence, the lemons principle and the scenario that good and bad products can be sold for the same price creates a welfare loss. Therefore, regulatory interventions with a view to reducing uncertainty, and providing tools for institutional evolutions have rooms here.

Next, a series of questions can be raised. They are not whether anti-regulation arguments still prevail but it is where to begin. And the lessons do not require us to go far. It is embodied in the modern history of accounting.

The reactions of policy makers to the great depression (1933/34) and the various stock market crashes (example 1987), the post-war reconstruction policies in Europe and Japan, the oil crises of the 1970s or other economic shocks either forced the establishment of regulatory bodies or the creation of new accounting rules [58, 62, 83]. This is the case even though there has been enough evidence both from euro-history [8] or otherwise [54] that a sort of voluntary disclosure(s) happened long before mandatory rules were established. More recently, after the end of the cold war, East Europeans are trying to replace their old (accounting) institutions with the myths and realities of market institutions. Hence, in sum, studying the history of these rule making bodies reveals that there had been some economically or politically significant events prior to the establishment of accounting institutions (law). Nowadays, the accounting laws of many nations provide detailed prescriptions as to the forms and contents of financial statements. With the increasing integration of economies, harmonization of accounting laws and practices has become the current preoccupation of many policy makers.

Consequently, these observations imply that the production of accounting information is not only likely to remain a regulated activity but is also showing signs of international rigidity. As a result, most self-regulation arguments and the option of leaving the production of accounting information to market forces become weaker not only in the context of Sub-Saharan economies but even in "modern" economies.

V. CONCLUSION AND DIRECTIONS FOR FUTURE RESEARCH

This paper has attempted to review the literature and discuss the merits of using regulatory tools for producing socially "optimal" level of accounting information. In doing so arguments from the anti-regulation side were addressed. Agency theory, informational efficiency of capital markets, private contractual opportunities and general scepticism about regulatory agencies have been examined. Agency theory has some potential to explain the upper sector of the economy. Thus, the existence of multiple stages in the SOE sector does not rule out the possibility of voluntary disclosures. However, whether it will serve as a policy instrument requires a further study.

On the side of pro-regulations, the public good nature of accounting information, failure of agent monitoring tools, asymmetry and speculation problems, moral hazard and adverse selection problems have been considered. A scenario based analysis of both sides of the arguments lead us to the conclusion that leaving the production of accounting information to markets became weaker, specially in Sub-Saharan environments. It follows then, for countries like Ethiopia, the option is not whether the market will solve the under-production of accounting information. It is how to strengthen and revise the laws (Commercial Code 1960, Proclamations Nos. 163/79 and 25/92) that are governing accounting practices and economic institutions.

Future research is hoped to examine the implications of adopting international regulations by using positive methods. Three policy paths are available. The first is to adopt the International Accounting Standards Committee's (IASC) standards. The second involves writing own rules with the risk of poor drafting and loss of reliance on published accounts internationally. The third is to establish a tiered system. One rule (IAS) for the upper section of the economy and another (local) for the lower sector. Accounting for institutional rearrangements (lease, valuations, privatisation), finding regulatory and institutional mechanisms for improving the activities of the informal sector, accounting for (peasant) agriculture, assessing the impacts of conventional accounting teachings/practices, estimating the direct and indirect costs of writing and implementing accounting regulations, are likely to shed some light.

Notes

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2. Gaa (1986:438) summarizes the main arguments for the establishment of standard setting bodies. To correct market failures (Godenes and Dopuch 1974, May and Sundrem 1976), to produce actions which are collectively rational (Avaizian and Callon 1983), to economize on contracting costs between firms, investors and creditors (Ng 1978), to promulgate standards that are in the interests of some economically or politically powerful groups possibly at the expense of weaker groups (Watts 1977, Jensen 1978, Watts and Zimmerman 1979).

3. While the dependencia theory in economics had created some audience, it is obvious that not much has been achieved in explaining the development-underdevelopment dichotomy.

4. About seventy-five percent of IASC standards are taken from FASB or British accounting standards mainly through product differentiation strategies. Many Sub-Saharan countries have adopted (partially) these standards.

5. See Copeland and Weston (1982:1-15) for reviews.

6. See Watts and Zimmerman (op cit) for example.

7. Nevertheless, in these research designs there are two hypothesises. The model and the hypothesis (that the market is efficient) are tested together. And it is difficult to separate which is which. See Beaver (1981) for more discussion on the issue.

Ceteris paribus, the counter argument that risk (beta) and cost of capital cannot be manipulated by the extent of disclosure/volume of information released for example through annual reports is also growing (Garsombeke 1979, Ohlson 1980, Negash 1990:1995). Reconciling the two seemingly conflicting reports requires a separate work.

8. Darrough and Stoughton (1988) for example note that firms can disclose voluntarily bad news about their activities to deter new entrants in product markets.

9. It should be noted that the existence of possible rivalries between the various (external) users of annual reports, does not necessarily change the public good nature of accounting information.

10. The concept that a seller of a product (example a security) will make (selectively) good news disclosure (to entice buyers) about his product is not something new. What is novel about the proprietary cost theorem is its attempt to provide analytical mechanism for the observed empirical regularity about the existence of voluntary disclosures.

Nevertheless, two problems arise in evaluating the theory. First there are few methodological guidelines for test designs. Scott's (1994) work on the labour relations of Canadian firms is the only evidence that (this author is aware of) are possible proprietary cost variables. Moreover, validation of the theory outside MDCs' environments is not an easy task. Secondly, the search for these variables may not go further than Watts and Zimmerman's (op cit) political cost variables.

11. For a summary of the issues involved, see Patel (1993).

12. Field (1981:175) describes markets as rules which presuppose at the minimum elementary guarantees against the use of force or fraud. White (1981:544) defines markets as "tangible cliques of producers observing each other" and notes that markets are shaped by trade-offs between dispersions, not by averages as suggested by the niche' that supply equals demand

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