Constituent lobbying and its impact on the development of financial reporting regulations: evidence from Germany

Stuart McLeay\textsuperscript{a,}*, Dieter Ordelheide\textsuperscript{b}, Steven Young\textsuperscript{c}

\textsuperscript{a}School of Accounting, Banking, and Economics, University of Wales, Bangor, UK
\textsuperscript{b}School of Business and Economics, J.W. Goethe-Universität, Frankfurt am Main, Germany
\textsuperscript{c}International Centre for Research in Accounting, Lancaster University, UK

Abstract

This paper examines the impact of constituent lobbying activity on accounting regulators during the transformation of the Fourth European Company Law Directive into German accounting law. Using detailed published commentaries prepared by representative organisations on draft accounting legislation, we provide evidence concerning the preferences of the three primary German constituencies—preparers, auditors, and academic experts. Initially, a model that merely distinguishes between the three constituencies suggests that the industry lobby group representing preparers exerts the greatest influence on the decisions of the German legislature. However, when the empirical model is extended to include all two-way interaction effects, the relative power of preparers is seen to be far lower, with the influence exerted by industry depending crucially on the support of at least one of the remaining lobby groups.

1. Introduction

The economic consequences of policy decisions make it impossible for accounting regulators to select non-controversial treatments on any of the issues they face based solely on technical considerations. Instead, the choice of appropriate accounting regulations reflects, at least in part, a social decision whereby regulatory bodies attempt to manage conflict between competing constituencies by selecting the most socially acceptable solution (Horngren, 1972; Sunder, 1988; Zeff, 1978). The political nature of accounting rule-development naturally raises questions concerning both the responsiveness of policy-makers to constituent pressure, and the distribution of power among competing interest groups. One means by which prior research has explored the source and extent of political influence in the context of accounting regulation is through the analysis of constituent lobbying activity. This study builds on extant research by examining public lobbying activity in Germany during the period when the Fourth European Company Law Directive (hereafter Fourth Directive) was transformed into German commercial law, the regulatory regime at the time being fundamentally different to that previously analysed.

Lobbying research in the accounting literature has focused almost exclusively on financial reporting regimes in English-speaking countries, most notably that of the US (Puro, 1984, 1985; Sutton, 1984; Tandy & Wilburn, 1992, 1996), and
to a lesser extent those of the UK (Hope & Gray, 1982; Nobes, 1991; Sutton, 1984), Australia (Klumpes, 1994; Walker & Robinson, 1994) and New Zealand (Rahman, Ng & Tower, 1994). While this body of work affords crucial insights into the nature of the standard-setting process, the institutional similarity of these regimes limits the generalisability of reported findings and provides little evidence as to the effect of the organisational form on the lobbying process. Examination of alternative regulatory environments is, therefore, warranted. In this context, the system operating in Germany until recently provided one of the most obvious examples of codified accounting regulation (Nobes & Parker, 1991, p. 12), where the legislature assumed primary responsibility for the development of financial reporting regulations, and where accounting rules were drafted by lawyers and administrators in the Ministries of Justice and Finance.

Implementation of the Fourth Directive represented a landmark in German accounting regulation, codifying as it did certain aspects of financial reporting which were already generally accepted in countries such as the US and UK. On the other hand, as a key element of the European Union’s harmonisation programme, the Fourth Directive also contained many aspects of German law which were then implemented elsewhere in Europe, i.e. the requirements for companies to adopt (i) defined methods of asset valuation and (ii) compulsory balance sheet and profit and loss formats. In the case of Germany, the provisions of the Fourth Directive were enacted into national law via the Accounting Directives Law (Bilanzrichtlinien-Gesetz), forming the legal basis for financial reporting for German companies. To obtain agreement on the provisions of the Fourth Directive at a European level, the document contained a large number of national options, affording member states significant flexibility over the transformation of many of its specific provisions. At a national level, the process of choosing between these various alternatives has provided a powerful setting within which to explore the political nature of accounting regulation.2

Using commentaries published by representative organisations during the transformation process, we identify the preferences of the three primary German accounting constituencies (industry, auditors, and academic experts) in relation to 169 separate financial reporting issues spanning aspects of valuation, recognition, disclosure and financial statement format. A striking feature of the approach adopted in Germany when the Fourth Directive was implemented is the manner in which representations made to the legislature reflected the collective view of the members of professional and industrial associations.

The relative influence of each of the lobby groups involved is assessed by examining the extent to which constituents’ stated preferences were ultimately reflected in the Accounting Directives Law. The approach used to identify lobbyists’ preferences is similar to that employed in extant research whereby lobbyists’ publicly available comments are classified as either ‘for’ or ‘against’ the associated exposure draft (e.g. Brown, 1981; Francis, 1987; Puro, 1984). Traditionally, such a coding procedure has proved problematic due to the relatively broad nature of both comment letter responses and the exposure drafts to which they pertain, resulting in the need for considerable judgement when reconciling the two (Puro, 1984). In contrast, because the German accounting rules under consideration were similar in structure to US tax code regulations, lobbyists’ proposals and the sections of commercial law to

---

1 Notable examples include the ‘true and fair view’ requirement and the need for increased disclosure.

2 Since this study examines only the transformation of the Fourth Directive into German national law, rather than the development of the Directive at a European level, it is possible that an additional dimension of the political process has been omitted from the analysis. At a national level, the transformation recommendations proposed by any lobby group(s) must have been developed within the framework of the Fourth Directive. Consequently, the framework of the Directive represents a significant external constraint on the regulatory process (Diggle & Nobes, 1994; Hussein & Ketz, 1991).

3 For example, Puro (1984) discusses the coding problems arising from cases in which respondents support one or more parts of an exposure draft while opposing or remaining silent on others.
which they refer were concise and highly specific in nature. This results in (i) greater objectivity with respect to the identification of lobbyists’ preferences and (ii) a more reliable measure of power (i.e. the extent to which these preferences are now reflected in commercial law).

A generalised linear model is used to assess how the German legislature incorporated constituents’ preferences in the regulations it promulgated. In addition to providing an appropriate means of modeling the relative influence of each lobby group in isolation, this approach enables a formal analysis of the way in which constituents’ preferences interact to determine policy outcomes. To the extent that the support of all sectors of the financial community is often seen as an essential element in the development of accounting regulations (Horn gren, 1972), the potential influence of any particular lobbyist is expected to be conditional, at least in part, on the position adopted by other lobby groups (Benveniste, 1972; Dyckman, 1988). To date, however, this issue remains relatively unexplored in the empirical literature. Initial findings for our main effects models suggest that, conditional on a proposal being made, industry exerted the greatest influence on the decisions of the legislature, while the odds of success associated with an academic proposal were significantly less than one. However, when the model is extended to include all two-way interactions between lobbyists, industry’s power is seen to have declined, with the outcome depending crucially on agreement between industry and one or more of the remaining lobby groups. Additional tests confirm that, rather than any single group’s preferences consistently dominating the legislature’s decisions, it was the existence of agreement among participant groups that ultimately determined the odds of success for a given proposal. As with the US, therefore, the process of accounting-rule development in Germany at the time of the implementation of the Fourth Directive appears to have been characterised by ‘power equivalency’ and the desire for political consensus.

In addition to empirically examining the politics of accounting rule-development within a fundamentally different and empirically more amenable regime to that previously considered, this study adds to the literature in three further respects. First, several commentators (e.g. Puro, 1984; Sutton, 1984) have suggested that the distribution of power among competing constituencies may vary as a function of the particular accounting issue under consideration. Because this study examines the politics of accounting rule-development across a wide range of accounting issues in relation to a single event, we are able to develop a more comprehensive model of accounting regulation than in prior work, where the focus has been largely restricted to the analysis of single (or small subsets of) accounting issues in isolation. We present results which suggest that power and influence are indeed conditional on the nature of the financial reporting issue: in particular, any relative influence that industry exerted on the legislature appears to have been restricted to disclosure issues.

Secondly, although the standard-setting process in many English-speaking countries has a strong private sector tradition, a degree of state intervention in regulatory initiatives remains a distinct possibility (Vieten, 1995; Wyatt, 1991).4 Even in Germany and France, which have seen the recent creation of standard-setting bodies, financial responsibility for accounting regulation remains within the state budget. The precise effect of these differing regulatory structures on the rule-development process remains ambiguous: for example, while Dyckman (1988) raises concerns over the susceptibility of public sector regulators to political pressure from those antagonistic to business, Sutton (1984) contends that the deliberations of private sector institutions are more susceptible to constituent influence due to their lack of legal mandate.5 To the extent that theoretical arguments

---

4 The FASB operates under the continual threat of increased Congressional involvement in the standard-setting process (Kirk, 1988). In the UK, recent changes to the standard-setting structure have resulted in the creation of a direct link between the Financial Reporting Council and the Department of Trade and Industry and while at present the UK government chooses to maintain a relatively passive stance, this position cannot be guaranteed in the future.

5 Further, Chatov (1985) argues that because bodies like the FASB act as agents of the network creating them, they are more likely to accede to the network’s wishes, and in the case of conflict are more likely to favour the preferences of the most powerful group.
alone cannot unambiguously delineate the potential costs and benefits of public sector involvement in the regulatory process, the issue is an empirical question. Comparison of the findings reported in this paper with the evidence documented for the US and similar systems highlights the existence of important commonalities across different institutional settings with respect to the accounting rule-development process.

Finally, the globalisation of business and the expansion of the capital markets has led to increasing pressure for accounting harmonisation and, by implication, a greater understanding of alternative financial reporting regimes. However, while many in the financial reporting community have resisted this pressure, choosing instead to focus attention on US standard-setting activity on the grounds that it is these standards which ultimately form the basis of international harmonisation efforts, the importance of alternative accounting approaches can no longer be denied (Wyatt & Yospe, 1993). Nowhere is this more clearly demonstrated than in the SEC’s decision to allow three international accounting standards (or parts thereof) to be accepted in cross border filings without reconciliation to US GAAP, even though the results produced by the application of these standards are substantially different from those produced under US GAAP (Bayless, Cochrane, Harris, Leisenring, McLaughlin & Wirtz, 1996). Evidence concerning both the process by which accounting rules are developed and the way in which these rules reflect constituents’ preferences, represents an important step towards understanding the product of alternative financial reporting regimes.

The remainder of the paper is organised as follows. The next section reviews extant lobbying research. We then present an overview of the institutional characteristics of accounting regulation in Germany at the time of the implementation of the Fourth Directive, together with details of the European accounting harmonisation programme.

2. Literature review

Using Downs’ (1957) model of voting, Sutton (1984) identifies the conditions under which rational lobbying will occur. Given a choice between two alternative proposals, lobbying is predicted in those circumstances where the differential wealth effect associated with the two proposals, discounted by the perceived probability of influencing the outcome, exceeds the cost of lobbying. Hence, the propensity for lobbying is hypothesised to be increasing in both (i) the magnitude of the perceived wealth effect and (ii) the expectation of influencing the final decision. To the extent that the potential economic consequences of securing a favoured proposal are thought to be greater in absolute terms for preparers than for users, evidence reported by Tandy and Wilburn (1992) for the US indicating that preparers are more active lobbyists than users serves to support Sutton’s first prediction. Similar lobbying patterns have been documented by Sutton for the UK and Walker and Robinson (1994) for Australia. In addition, the significant financial interest of audit firms in their clients’ welfare helps explain the relatively high lobbying propensity observed for large US public accounting firms, while the low levels of lobbying observed for US accounting academics has been partly attributed to the lack of a significant wealth effect (Tandy & Wilburn, 1996). Further, intra-industry studies indicate that the likelihood of an individual firm engaging in lobbying activity is also positively associated with the magnitude of the perceived wealth effects (e.g. Francis, 1987; Griffin, 1983; Kelly, 1982, 1985; Watts & Zimmerman, 1978). Tandy and Wilburn (1996) also document direct evidence in support of Sutton’s second prediction. Specifically, they find that one of the main reasons cited by US academics against active participation in the FASB’s due process procedures is their perceived low probability of success. However, since

6 The International Accounting Standards (IASs) permitted by the SEC in cross border filings are IAS 7: Cash Flow Statements, parts of IAS 21: The Effects of Changes in Foreign Exchange Rates and IAS 22: Business Combinations. Further, IASs are now accepted by the London Stock Exchange for cross-border listings.
prior research has focused almost exclusively on the type of financial reporting system prevalent in English-speaking countries, little evidence exists to support Sutton’s additional assertion that these predictions will hold irrespective of the institutional setting within which accounting regulations are developed.

While the benefit term in Sutton’s lobbying equation is expected to vary between preparers and users in general, it may also differ across alternative accounting issues for any preparer–user combination (Sutton, 1984), suggesting that constituent lobbying propensity may be affected by the scope and nature of the accounting issue under consideration. For example, Tandy and Wilburn (1992) document greater lobbying activity by the industry and academic constituent groups on substantive standards compared with both industry standards and amendments. Similarly, substantive standards elicited a greater mean number of submissions from public accounting firms than for industry standards. Further, Puro (1984) provides evidence that the extent of preference alignment between preparer and auditor lobby groups may also differ according to the underlying nature of the accounting issue: preparers and auditors are more likely to adopt similar lobbying positions in relation to proposals designed to standardise accounting treatments, whereas they tend to adopt competing positions in relation to issues of disclosure. To the extent that agreement among two or more groups results in a multiplier effect, whereby the combined influence of the coalition is significantly greater than the influence of a single group acting alone (Benveniste, 1972; Dyckman, 1988), Puro’s findings suggest that constituent influence may also vary as a function of the nature of the financial reporting issue under debate. To date, however, this issue remains largely unexplored in the empirical literature.

Several studies (e.g. Brown, 1981; Hussein & Ketz, 1980; Newman, 1981; Puro, 1985) have used lobbying data to investigate the impact of pressure groups on the policy decisions taken by standard-setting agencies following allegations in the Metcalf report (US Congress, 1976) that the FASB was unduly influenced in its policy-making process by certain sectors of society (primarily the large audit firms and their clients). However, the evidence reported in these studies suggests that the FASB’s policy decisions are not consistently dominated by any single group or coalition of groups. Instead, results suggest the influence of many centers of power. Indeed, Hussein and Ketz (1991) conclude that the FASB’s deliberations are characterised by a system of ‘power equivalency’, whereby the structural and relational contracts make it impossible for any single agent or coalition of agents to dominate the process. Similar conclusions are presented by Hope and Gray (1982) in relation to the UK standard-setting process. While this body of work provides important evidence concerning the political nature of accounting regulation, Hussein and Ketz (1991) argue that power and influence are determined, at least in part, by the prevailing regulatory structure. Consequently, different regulatory structures may be associated with different political outcomes. A broader understanding of the politics of accounting regulation therefore demands the analysis of alternative regulatory systems.

3. Institutional background

Traditionally, decisions on accounting rules have been viewed in Germany not only as a technical matter on which a group of accounting experts should be competent but also as an issue of public policy having a relatively broad social basis (Ordelheide & Pfaff, 1994, p. 82). The resulting law-based system of financial reporting is primarily dependent on commercial law, with strong connections to tax law, and this is still the case following the recent reform which established a body to develop German accounting standards. Until 1985, the Stock Corporation Law (Aktiengesetz) of 1965 represented the primary source of

---

7 The strong association between financial reporting and tax accounting is the result of the *Maßgeblichkeitsprinzip* which requires that the statutory accounts form the authoritative basis for taxation and the ‘reverse authoritativeness principle’ (*umgekehrte Maßgeblichkeitsprinzip*), which requires that tax rules must be observed in commercial accounts in order to benefit from tax incentives.
accounting requirements for listed companies, supplemented by provisions in the Commercial Code (Handelsgesetzbuch) and income tax law. Following the transformation of the Fourth (and Seventh) Directive into German commercial law in 1985, the Accounting Directives Law became the legal basis for financial reporting in Germany. The Accounting Directives Law amended the Commercial Code, the latter containing the general accounting and auditing rules applicable to all companies, together with a special section relating to stock corporations and limited liability companies.

While the Accounting Directives Law codified many important accounting principles and standards, the German legal provisions are not exhaustive. For example, foreign currency translation and accounting for leasing and government grants are not regulated explicitly in the Commercial Code. In the absence of such regulations, companies have resorted to tax law and tax court rulings for authoritative and legally-binding interpretations of the Commercial Code. Additionally, certain non-authoritative legal interpretations are combined with authoritative rulings to form the ‘Correct Accounting Principles’ (Grundsätze ordnungsmäßiger Buchführung or GoB) explicitly referred to in the Commercial Code.9 This combination of legislative rules and legal interpretations provides a distinctive hierarchical structure to accounting regulation in Germany (Ordelheide, 1999), creating two primary mechanisms through which parties have been able to shape financial reporting practice. First, agents have influenced commercial law directly by lobbying the legislative body during the rule-development process. Such participation by representative bodies in law-making has constituted an important part of the due process of accounting regulation in Germany, actively encouraged by the legislature. Second, agents can contribute to the market for legal interpretations. Law commentaries and interpretative articles which seek to clarify legal requirements have been produced regularly by barristers, judges, auditors, experts from business and the public sector, and academics.10 Until now, the complete system of legal interpretations has been collected together and published in law commentaries and financial accounting handbooks [e.g. Adler-Düring-Schmaltz (Forster, 1997)].

Reflecting the codified approach to regulation in Germany, the accounting rule-development process was coordinated until recently by the Ministry of Justice. In contrast with the Anglo–American approach, only a relatively minor role was ascribed to the audit profession, for which the traditional emphasis was concerned with clients’ compliance with the law rather than with the development of binding accounting principles and procedures.11 While accounting in Germany has been influenced by a wide range of other parties, including private research institutes, academic accountants, preparer groups organised by the Confederation of German Industries, and the audit profession, the financial reporting regulations examined in this study were drafted by lawyers and administrators in the Ministries of Finance and Justice.

---

8 No additional specific regulations existed for alternative corporate forms such as limited liability companies or for non-corporations such as partnerships and sole traders.

9 The GoB has been interpreted as meaning ‘those principles which are not comprehensively codified but which, by application in specific cases, lead to a correct accounting treatment by reference to the objectives of financial statements. They can be determined deductively by making full use of statute and case law, accounting theory, pronouncements of the Institute of Auditors, as well as accounting practice’ (Brooks & Mertin, 1986).

10 For example, the Institute of Auditors (Institut der Wirtschaftsprüfer) regularly publishes opinions on legislative pronouncements, laws, and contemporary financial accounting and auditing issues. While these opinions are not legally binding, the risk of an auditor being accused of professional malpractice is higher if an auditor has certified financial statements that are in conflict with such recommendations (Ordelheide, 1999).

11 Whereas in the US, performance of the audit function is not a prerequisite for affiliation to the AICPA, membership of the Institute of Auditors is confined to practising auditors only. This distinction reflects fundamental differences in the role attributed to the profession in each country: in the US, the audit profession assumes significant responsibility for the development of accounting standards; by contrast, the German audit profession operates within a more tightly defined jurisdiction, where the emphasis rests firmly on performance of the statutory audit function (Vieten, 1995).
3.1. European accounting harmonisation and the Fourth Directive

An objective of the European Union is the convergence not only of economic conditions but also of member states’ respective national laws to the extent required for the common market to function in an orderly manner. To achieve this aim, a programme of legal harmonisation has been implemented involving the development of a series of Company Law Directives. When the European Commission has obtained agreement on a set of proposals relating to the harmonisation of a particular topic, it places a Draft Directive before the Council of Ministers. If the Directive is adopted, governments of the member states have a specified period in which to enact the legislation and incorporate the Directives’ provisions into their national law. To obtain agreement at a European level, it is usual for a Directive to contain a range of national options, according member states significant flexibility when enacting its provisions into national law. It is the choice among these national options with respect to the Fourth Directive that provides the background to our analysis of accounting regulation in Germany.

Integration of the provisions of the Fourth Directive into German law began with the publication of the legislature’s transformation recommendations. Comments on this document were invited from all interested parties in Germany and used by the Ministries of Justice and Finance to produce a pre-draft law. Five subsequent draft laws were published prior to enactment of the Accounting Directives Law in December 1985 and comments were received following each stage. While 27 organisations were officially invited to comment during the drafting stage, only industry, academia and the audit profession engaged in formal lobbying on a material number of accounting issues and on successive drafts of the law. The restriction of lobbying activity to this limited set of financial reporting experts reflects, at least in part, the highly complex nature of German commercial law and the resulting barriers to entry this creates. The absence of formal lobbying activity by user associations may be partially explained by the decision of the German banks (the primary users of financial reporting information) to adopt a preparer position for lobbying purposes. The greater involvement of preparers relative to users in the lobbying process is also consistent with both Sutton’s (1984) theoretical model of lobbying activity and with Tandy and Wilburn’s (1992) study of constituent lobbying of the FASB.

Lobbying was conducted both publicly in the form of published commentaries and submissions to official hearings, and privately in the form of unpublished letters and informal discussions. Reflecting both the collectivist nature of German society (Power, 1997) and cost efficiencies associated with organised lobbying activity (Sutton, 1984), all formal proposals were issued through representative agencies. The preparer viewpoint was represented by the Association for Finance and Management (Gesellschaft für Finanzwissenschaft in der Unternehmensführung) and the Combined Associations of German Industry (Spitzenverbände der deutschen Wirtschaft). Proposals from each association were developed by a series of working parties, membership of which was drawn from the corporate sector, and published in the journal Der Betrieb. The audit profession’s viewpoint was jointly represented by the Institute of Auditors (Institut der Wirtschaftsprüfer) and the Chamber of Auditors (Wirtschaftsprüferkammer). Proposals were drawn up by working groups, issued as professional opinions, and published at the outset in Der Betrieb and later in Die Wirtschaftsprüfung. Finally, the

---

12 The former is a private organisation of senior accounting and finance managers from the large German corporations, while the latter is an umbrella organisation for various business associations, including representatives from the retail, banking, and small firm sectors. For the purpose of enacting the Fourth Directive, the following groups were involved: the Federation of German Industries; the Association of German Industry and Commerce; the Federation of German Wholesale and Foreign Trade; and the Federation of German Banks (Ordelheide, 1999).


academic position was represented by the Accounting Committee of the Association of German Business Studies Academics (Kommission Rechnungswesen im Verband der Hochschullehrer für Betriebswirtschaft). Formed in 1977 specifically to facilitate academic participation in the process of transforming European Company Law Directives into German law, the Committee appointed two working groups to debate the draft legislation. The results of these debates were then submitted to the Committee and, after subsequent modification, published as official opinions in *Die Betriebswirtschaft*.15

4. Data and sample

Empirical tests are conducted using commentaries published by the representative bodies identified in Section 3.1 during the draft law stages of the transformation process.16 For all accounting issues examined, both industry associations made identical proposals. To simplify the empirical analysis and increase model parsimony, we aggregate these two associations to form a single industry group, denoted IND. Similarly, because the Institute of Auditors and the Chamber of Auditors acted in unison throughout the transformation process (Ordelheide, 1999), we aggregate these two parties to form a single auditor group, denoted AUD. Proposals made by the Accounting Committee of the Association of German Business Studies Academics are denoted ACA.

For each lobby group (IND, AUD and ACA), all publicly available comments were surveyed to identify each formal proposal. A total of 169 separate issues covering aspects of valuation, recognition, disclosure and financial statement format were identified on which at least one of the three groups commented formally.17 The nature of these proposals was such that they clearly indicated (i) the specific legal provision under discussion and (ii) the lobbyist’s proposed accounting treatment.

Consistent with much of the extant literature on accounting regulation, we adopt a pluralist model as a means of operationalising the concept of political power.18 Within this framework, power is assessed by distinguishing those lobbyists whose proposals are ultimately adopted (i.e. successful) from those whose proposals are rejected (i.e. unsuccessful). Lobbyists with the highest proportion of ‘successes’ are then considered to exhibit the greatest political influence while those with the lowest proportion are assumed to be the least influential. For the 169 issues on which at least one of the three groups proposed a change to the law, the proposals were compared with the legal requirement contained in the final text of the Accounting Directives Law. For each constituent, a recommendation corresponding to the accounting treatment ultimately required by the Accounting Directives Law is categorised as ‘successful’. Alternatively, a recommendation which fails to correspond with the treatment required by the Accounting Directives Law is assumed to have been ‘unsuccessful’. Finally, in the event that a lobbyist makes no formal (i.e. publicly available) proposal on a particular issue, an absence of lobbying activity is inferred.

The procedure described above provides a relatively objective measure of the extent to which lobbyists’ proposals are ultimately realised by the legislature in commercial law. Admittedly, as the approach relies on final outcomes to generate the observable counts of ‘successes’, it does not allow for a detailed investigation of strategic lobbying behaviour in a multi-period framework where

---

16 Consistent with prior work, this study focuses on observable lobbying behaviour. To the extent that private lobbying was either more influential than public lobbying, or differed in respect to the nature of the preferences expressed, the results of this study should be interpreted with caution.

17 Of the 169 points of accounting law identified, 46 related to issues of valuation, 46 to issues of recognition, 36 to issues of financial statement format and 41 to issues of disclosure.

18 The pluralist model of power has been the subject of significant criticism [see Lukes (1974) and Walker and Robinson (1993) for a discussion]. However, in defence of the pluralist model, Lukes (1974) acknowledges that in many cases it represents the most useful method of operationalizing and analysing power.
there may be variation in the level of interest with respect to individual points of law. Nevertheless, the database provides a unique setting in which to estimate lobbyist influence and to assess the overall impact on such influence of agreement and disagreement between lobbyists. Indeed, an important aspect of constituent lobbying is that success depends not only on each interest group’s own actions but also on the degree of consensus and conflict among the participant groups (Bveniste, 1972). An explicit consideration of the interaction between lobbyists’ stated preferences therefore seems appropriate. A limitation of our data, however, is that when two or more parties submit similar proposals, we are unable to distinguish between those cases which arise as a result of an explicit coalition and those cases where it represents two independently determined positions. Consequently, when modeling lobbyists’ interactions, we define ‘agreement’ simply as the stylised fact that two equivalent proposals have been made, while ‘disagreement’ is defined as the presence of a proposal and a counterproposal. Further, an implication of the participation of three lobby groups in the rule-development process is the occurrence of situations where two of the interest groups make the same proposal while the third makes a counterproposal. We model such situations as a set of two-way interactions comprising one case of agreement (e.g. between IND and AUD) and two separate cases of disagreement (between IND and ACA and between AUD and ACA). Finally, an additional characteristic of the data is that in the case of disagreement, one of the proposals always becomes law. That is, conflict amongst lobby groups always leads to success for one or more of the parties involved. On the other hand, uncontested proposals made by one, two or three parties may fail to become law. Here, the lobbying process in Germany is modelled on the basis of these stylised facts.

Table 1 presents the observed frequencies of success, failure and non-participation, cross-classified by lobby group. The three lobby groups made a total of 269 proposals, 148 of which were successful. The draft law was amended by the regulator with respect to 63% of the issues on which comments were made (i.e. 106 issues out of 169). When only one of the lobbying groups made a proposal, less than half (43 of 97) of the respective regulations were revised. In contrast, the regulator changed the legal text in 63 of the 72 issues which attracted proposals from more than one lobby group. In summary, the conditional probability that a proposal would be successful if made by just one lobbying group was only 0.443, but it was as high as 0.875 if made by more than one lobbying group.

A fuller understanding of these success probabilities requires an approach which controls not only for conditioning factors such as the differences between the parties in the odds of making a proposal in the first place but also for the likelihood of agreement or disagreement over the nature of the proposed amendment to the law. In the latter case, these probabilities can be estimated either for the general case (i.e. that there exists agreement or disagreement, or both, over an issue) or the specific (i.e. that two parties in particular agree or disagree). In this way, an idea can be gained not only of the odds that a proposal will succeed but also of how such odds vary across the parties when they agree or disagree. In this paper, we refer to the odds of making a proposal as \( \theta \) and to the odds that it will succeed as \( \omega \), whilst agreement is denoted by \( \phi \) and disagreement by \( \varphi \). A more detailed discussion of model development in this context is given below, followed by the empirical results.

5. Model specification

The count in each cell of Table 1 follows a multinominal frequency distribution with unknown probabilities (Francis, Green & Payne, 1993). A statistical model to estimate the probability structure of this data may be written in the form of a generalised linear model (Nelder & Wedderburn, 1972). For situations in which the response variate is a vector of frequencies from a multi-way contingency table and the explanatory variables are categorical (i.e. no proposal, proposal accepted, or proposal rejected), McCullagh and Nelder (1989) demonstrate that the appropriate formulation is a log-linear model with a log link function and a Poisson distributed error. Under this scheme, the count in a given cell may be expressed as a function
of the main effects (subscripted IND, AUD, and ACA) and the associated interactions. As well as this approach representing the most appropriate modeling procedure given the nature of the data, it affords the additional advantage of facilitating an explicit analysis of the way in which individual lobbyists’ preferences interact in determining German accounting law.\(^{19}\)

The standard approach in log-linear modeling assumes that hierarchical models are to be fitted, such that the existence of a higher-order interaction necessarily implies the inclusion of all lower order terms marginal to it (Francis et al., 1993, p. 249). We therefore fit a number of levels of the model to account for the extent of agreement or disagreement, the relative influence of the individual lobbying organisations, the odds of success when such consensus and conflict exists, and finally, the effect on those odds of the mix of parties involved.

---

\(^{19}\) Since our interest is restricted to those issues on which at least one of the three lobbyists made a proposal, the corner cell IND = ACA = AUD = 0 is treated as a structural zero (Francis et al., 1993, p. 272).

---

**Table 1**
Constituent lobbying activity in relation to the transformation of the Fourth Directive into German commercial law, cross-classified by constituent group and lobbying outcome\(^{a,b}\)

<table>
<thead>
<tr>
<th>Academics = No proposal</th>
<th>Auditors</th>
<th>Industry</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No proposal</td>
<td>Accepted</td>
</tr>
<tr>
<td>Accepted</td>
<td>0</td>
<td>22</td>
</tr>
<tr>
<td>Rejected</td>
<td>11</td>
<td>3</td>
</tr>
<tr>
<td>Total</td>
<td>24</td>
<td>35</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Academics = Accepted</th>
<th>Auditors</th>
<th>Industry</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No proposal</td>
<td>Accepted</td>
</tr>
<tr>
<td>Accepted</td>
<td>8</td>
<td>5</td>
</tr>
<tr>
<td>Rejected</td>
<td>3</td>
<td>6</td>
</tr>
<tr>
<td>Total</td>
<td>11</td>
<td>12</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Academics = Rejected</th>
<th>Auditors</th>
<th>Industry</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No proposal</td>
<td>Accepted</td>
</tr>
<tr>
<td>Accepted</td>
<td>21</td>
<td>10</td>
</tr>
<tr>
<td>Rejected</td>
<td>0</td>
<td>8</td>
</tr>
<tr>
<td>Total</td>
<td>23</td>
<td>26</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Academics = Total</th>
<th>Auditors</th>
<th>Industry</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No proposal</td>
<td>Accepted</td>
</tr>
<tr>
<td>Accepted</td>
<td>29</td>
<td>37</td>
</tr>
<tr>
<td>Rejected</td>
<td>16</td>
<td>24</td>
</tr>
<tr>
<td>Total</td>
<td>58</td>
<td>73</td>
</tr>
</tbody>
</table>

\(^{a}\) The sample consists of 169 separate accounting issues on which at least one constituent group (i.e., industry, auditors, or academics) lobbied the German legislature. For each accounting issue, lobbyists’ proposals were compared with the ultimate legal requirement contained in the Accounting Directives Law. Proposals corresponding to the Accounting Directives Law requirement were considered successful and coded ‘accepted’, while proposals which did not correspond with the Accounting Directives Law requirement were considered unsuccessful and coded ‘rejected’. In the event that a lobbyist made no formal (i.e., publicly available) proposal on a particular issue, an absence of lobbying activity was inferred.

\(^{b}\) The industry constituency was represented by two organisations: The Association for Finance and Management and the Combined Associations of German Industry. Since both organisations adopted the same lobbying position, for all 169 cases examined we aggregate these two associations to form a single industry group. The auditor constituency was jointly represented by the Institute of Auditors and the Chamber of Auditors on all 169 cases examined. These two parties are again aggregated to form a single auditor group. Finally, the academic constituency was represented by the Accounting Committee of the Association of German Business Studies Academics.
5.1. Conditional independence

The lowest order log-linear model is that of complete independence, where the expected value is equal in each cross-classified cell, except for the structural zero in the corner cell where none of the lobbyists makes a proposal. However, since this simplistic model is unlikely to provide any material insights into the structure of our data, we begin by fitting a model where the probabilities of making a proposal are allowed to vary across the constituent groups. We refer to this initial model as the model of conditional independence, since the estimates of expected acceptances and rejections are conditional on a proposal having been made but are independent of the relative influence of the lobbyists and any possible interactions between them. The model of conditional independence therefore represents the null against which each group’s relative influence, and the impact of agreement and disagreement, may be assessed. For the model of conditional independence, the log of the observed count may be generalised as

\[ \log C_0 = \sum_i \theta_i x_i. \]

where:
- \( C_0 \) = a vector of observations representing the observed counts, \( C_i \) in Table 1, adjusted for the mean effect;
- \( \theta_i \) = the log-odds that lobby group \( i \) makes a proposal;
- \( x_i \) = the industry (IND), auditor (AUD), or academic (ACA) lobby groups.

For each lobby group \( i \), \( \theta \) is defined as a two-level factor, taking the value one if \( i \) made a proposal and zero otherwise.

5.2. Relative influence

This model evaluates the unconditional odds of success for each of the lobbyists. In this case, the log of the mean-adjusted observed count is

\[ \log C' = \sum_i \theta_i + \sum_i \omega_i. \]

where:
- \( \omega_i \) = the log-odds that a proposal made by lobby group \( i \) will be accepted.

All other variables are as previously defined and, for each lobby group \( i \), \( \omega_i \) is defined as a two-level factor, taking the value one if \( i \)'s proposal was successful and zero if it was rejected.

5.3. Agreement and disagreement

Adding the main effects of agreement and disagreement to model (2) generates the following model:

\[ \log C' = \sum_i \theta_i + \sum_i \omega_i + \phi + \varphi \]

where:
- \( \phi \) = the overall log-odds that two parties will make the same proposal, defined as a two-level factor taking the value one if any two lobbyists make the same proposal, and zero otherwise;
- \( \varphi \) = the overall log-odds that two proposals differ, defined as a two-level factor taking the value one if any two lobbyists make different proposals on a given accounting issue, and zero otherwise.

While model (3) is expressed as a main effects model, interaction terms can also be included to account for those cases where two lobbyists are in agreement while the third seeks a different outcome (i.e. \( \phi \cdot \varphi \)), and also for the log odds that an identical proposal put forward by more than one party will lead to a change in the law (i.e. \( \omega \cdot \phi \)). At the general level, the interaction between disagreement and success (\( \omega \cdot \varphi \)) remains constant in this study, since for each case involving conflicting proposals, one of the proposals always became law.

5.4. Agreement and disagreement with lobby group \( i \)

The generalised models presented above can be rewritten to allow for the relative odds of agreement or disagreement with the \( i \)th lobby group, as follows:

\[ \log C' = \sum_i \theta_i + \sum_i \omega_i + \sum_i \phi_i + \sum_i \varphi_i \]
where:
\( \phi_i \) = a two-level factor taking the value one when a proposal put forward by lobby group \( i \) is in agreement with any other proposal, and zero otherwise;
\( \phi_j \) = a two-level factor taking the value one when a proposal put forward by lobby group \( j \) is in disagreement with any other proposal, and zero otherwise.

Model (4.1) may also be extended by including interaction terms to account for the relative odds of success when there is agreement and disagreement. This extended model is written as

\[
\log C' = \sum_i \theta_i + \sum_i \omega_i \phi_i + \sum_i \omega_i \varphi_i
\]

where:
\( \omega_i \phi_i \) = the sum of the main effects that a proposal made by lobbyist \( i \) will be successful and that a similar proposal to lobbyist \( i \)'s will be made by another lobby group, plus the interaction effect on the success of a proposal by lobbyist \( i \) when a similar proposal has been made by another lobby (i.e. \( \omega_i \phi_i = \omega_i + \phi_i + \omega_i \cdot \phi_i \));
\( \omega_i \varphi_i \) = the sum of main and interaction effects of a successful counterproposal from lobbyist \( i \) (i.e. \( \omega_i \varphi_i = \omega_i + \varphi_i + \omega_i \cdot \varphi_i \)).

5.5. Agreement and disagreement between lobby groups \( i \) and \( j \)

The final model allows for each of the possible two-way cases of agreement and disagreement between each pair of lobbyists \( i \) and \( j \), where \( i \neq j \). This model may be specified as

\[
\log C' = \sum_i \theta_i + \sum_i \omega_i \phi_i + \sum_i \sum_j \phi_{ij} + \sum_j \sum_i \varphi_{ij}
\]

(5.1)

where:
\( \phi_{ij} \) = a two-level factor taking the value one when \( i \) and \( j \) are in agreement, and zero otherwise;
\( \varphi_{ij} \) = a two-level factor taking the value one when \( i \) and \( j \) are in disagreement, and zero otherwise.

Finally, the relative odds of succeeding in changing the draft law when there is either agreement or disagreement between \( i \) and \( j \) may now be added as interactions. The odds of success for lobbyist \( i \) are given by \( \omega_i \cdot \phi_{ij} \) in the case where the proposals put forward by \( i \) and \( j \) are the same, and by \( \omega_i \cdot \varphi_{ij} \) where they differ, giving the following model:

\[
\log C' = \sum_i \theta_i + \sum_i \sum_j \omega_i \phi_{ij} + \sum_i \sum_j \omega_i \varphi_{ij}
\]

(5.2)

where:
\( \omega_i \phi_{ij} \) = the sum of the main effects that a proposal made by lobbyist \( i \) will be successful and that a similar proposal to lobbyist \( i \)'s will be made by lobby group \( j \), plus the interaction effect on the success of a proposal by lobbyist \( i \) when groups \( i \) and \( j \) put forward the same proposal;
\( \omega_i \varphi_{ij} \) = the sum of the main effects that a proposal made by lobbyist \( i \) will be successful and that a counter proposal to lobbyist \( i \)'s will be made by lobby group \( j \), plus the interaction effect on the success of a proposal by lobbyist \( i \) when groups \( i \) and \( j \) make conflicting proposals.

Since the relative odds of success when \( i \) and \( j \) are in agreement are necessarily identical for the two parties involved, the interaction terms \( \omega_i \cdot \phi_{ij} \) and \( \omega_j \cdot \phi_{ij} \) are equal. In contrast, since the relative odds that lobby group \( i \) will win a contest with \( j \) are the inverse of the relative odds that lobby group \( j \) will win, \( \omega_i \cdot \varphi_{ij} \) is equivalent to \( -\omega_j \cdot \varphi_{ij} \).

A summary of the hierarchy of main effects models and their associated factor structure is presented in Table 2.

5.6. Goodness of fit

The appropriate measure of goodness of fit for a log-linear model with a Poisson error is the deviance (D). The deviance compares the maximised log-likelihood for the \( n \)th fitted model (\( m_n \)) and the fully saturated model and provides a general test of the adequacy of the fitted model.\(^{20}\)

\(^{20}\)A significant value for the deviance indicates that a significant term has been omitted from the model. For the Normal model, the deviance is equal to the residual sum of squares, while in the case of the Poisson model it has an interpretation similar to the Pearson goodness of fit statistic (Francis et al., 1993, p. 275).
Accordingly, the relative goodness of fit of two nested models \((m_1\) and \(m_2\)) is measured as the difference between their associated deviances \((D_1 - D_2)\) where \(m_1\) is nested in \(m_2\). \(D_1 - D_2\) is asymptotically chi-squared distributed with \(d_1 - d_2\), degrees of freedom. A significant value for \(D_1 - D_2\) indicates that \(m_2\) is a better model than \(m_1\) or equivalently, that the terms omitted from \(m_1\) are significant. The appropriate F-ratio compares the mean change in deviance \((D_1 - D_2)/(d_1 - d_2)\) and the mean residual deviance \((D_2/d_2)\), and is distributed \(F \sim [(d_1 - d_2), d_2]\).

6. Empirical results

Model (1) reflects the propensity for a particular lobbyist to submit a proposal. The coefficients\(^{21}\)

\(^{21}\) The \(\hat{\theta}_t\) estimates from model (1), representing the log-odds that lobby group \(i\) will make a proposal, were as follows: \(\hat{\theta}_{\text{ND}} = 3.034\) \((t = 2.98)\); \(\hat{\theta}_{\text{AUD}} = 2.314\) \((t = 7.62)\); \(\hat{\theta}_{\text{ACA}} = 2.479\) \((t = 6.61)\). T-tests for the significance of individual parameter estimates are based on the assumption of a symmetric likelihood function. Reported \(t\)-statistics represent only a guide to the significance of a particular parameter with respect to a null of zero, rather than indicating the relative likelihood, and must therefore be interpreted with caution.
from the model of conditional independence provide evidence of industry’s high submission rate and the low level of public involvement by the German audit profession in the rule-development process: industry submitted proposals on 111 of the 169 issues examined (66% proposal rate) compared with 75 proposals submitted by the audit profession (44% proposal rate). Further, German accounting academics are seen to display a higher propensity for public lobbying than the audit profession, in contrast to the findings documented for the US and similar regimes. While this result may partly reflect the German auditor’s traditional concern for the application of financial reporting rules, rather than for the development of these rules (Vieten, 1995), the high level of public lobbying activity observed for German accounting academics may result from the evolution of the legal perspective as the dominant research approach to date in Germany, whereby accounting researchers have been actively involved in a form of jurisprudence, by interpreting existing laws where doubts have arisen.\footnote{In serving the market for interpretations, some academics will derive support from audit firms or direct from industry. In this respect, they are not necessarily disinterested individuals who serve merely to interpret the law. However, participation in the process of redrafting the law is through the auspices of an academic body which acts on behalf of the German academic profession as a whole, not individual academics.}

Table 3 presents tests of the change in deviance for the hierarchy of models discussed above, along with the estimated coefficients. The change in deviance associated with fitting model (2), which provides evidence as to the relative power of the three lobby groups, is not significant at conventional levels ($p=0.241$). However, it is notable that the odds of success are significantly greater than one for industry (log-odds=-0.652; odds=1.92:1; $t=3.27$) and significantly less than one for the academic experts (log-odds=-0.466; odds=1:1.59; $t=-2.07$). These findings reflect the fact that industry succeeded in 73 out of 111 proposals submitted (i.e. 63%) whereas the academics succeeded in only 32 of their 83 proposals (i.e. 38%). The insignificant coefficient estimate on the $\omega_{\text{AUD}}$ term indicates that the odds of success for the audit profession were approximately equal to one. Examination of the results documented in panel B of Table 3 confirms that, after accounting for the general effects of agreement ($\phi$) and disagreement ($\bar{\phi}$), industry’s odds remain significantly greater than one ($t=3.31$), while the odds of success for the auditor constituency remain equal to one and those for the academic constituency are again significantly less than one. In sum, the findings for models (2) and (3) suggest that German industry exerted most influence over the legislature during the transformation of the Fourth Directive into commercial law. In contrast, the influence of the academic community appears to have been relatively low, despite their active participation.

Extension of model (3) to include the general interaction term $\omega \cdot \phi$, which accounts for the log-odds of success given agreement between any two lobby groups, provides further insights into the politics of accounting rule-development in Germany. The positive and significant coefficient on $\omega \cdot \phi$ ($t=2.65$) indicates that the overall odds of success are increased by more than 2:1 when any two groups take similar positions with respect to a particular financial reporting issue, reinforcing the view that the responsiveness of the German legislature is a positive function of consensus among lobby groups. The findings for Germany that agreement among constituent groups has been an important factor influencing the decision of the legislature is consistent with the views expressed with respect to the US by Dyckman (1988) and Horngren (1972), both of whom argue that the search for political consensus underlies many of the financial reporting solutions proposed by the FASB.

Models (4.1) and (4.2) account for the relative odds of agreement or disagreement with the $i$th lobby group. Panel C of Table 3 reports a significant and positive estimate of $\phi_{\text{AUD}}$ ($t=3.14$) under the main effects model (4.1), suggesting a high likelihood that lobbying by auditors would have been accompanied by consensus. This effect alone, however, does not change the measures of relative influence, with industry continuing to appear more successful than the other groups. Model (4.2) extends model (4.1) by including interaction terms which account for the relative odds of success when there is agreement or
Table 3
The relative influence of constituent lobby groups in Germany (t-statistics in parentheses)a

Panel A: Relative influence

<table>
<thead>
<tr>
<th>Relative influence of lobby group i</th>
<th>Deviance</th>
<th>ΔDevianceb</th>
<th>Fc</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>IND</td>
<td>0.652</td>
<td>0.295</td>
<td>0.466</td>
<td>71.747</td>
</tr>
<tr>
<td>AUD</td>
<td>(3.27)</td>
<td>(1.27)</td>
<td>(−2.07)</td>
<td></td>
</tr>
<tr>
<td>ACA</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Panel B: Agreement and disagreementd

<table>
<thead>
<tr>
<th>Relative influence of lobby group i</th>
<th>Agreement (φ) and disagreement (ψ)</th>
<th>Deviance</th>
<th>ΔDeviance</th>
<th>Fc</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>IND</td>
<td>0.665</td>
<td>0.279</td>
<td>−0.518</td>
<td>53.515</td>
<td>18.232(2, 3)</td>
</tr>
<tr>
<td>AUD</td>
<td>(3.31)</td>
<td>(1.39)</td>
<td>(−2.25)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ACA</td>
<td>(−2.54)</td>
<td>(−3.55)</td>
<td>(−1.70)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Panel C: Agreement and disagreement with each lobby group

<table>
<thead>
<tr>
<th>Relative influence of lobby group i</th>
<th>Agreement (φ) and disagreement (ψ) with i = IND</th>
<th>Agreement (φ) and disagreement (ψ) with i = AUD</th>
<th>Agreement (φ) and disagreement (ψ) with i = ACA</th>
<th>Deviance</th>
<th>ΔDeviance</th>
<th>Fc</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>IND</td>
<td>0.393</td>
<td>0.238</td>
<td>−0.411</td>
<td>0.613</td>
<td>1.129</td>
<td>1.243</td>
<td>−0.675</td>
</tr>
<tr>
<td>AUD</td>
<td>(2.92)</td>
<td>(0.99)</td>
<td>(−1.78)</td>
<td>(1.57)</td>
<td>(1.75)</td>
<td>(3.14)</td>
<td>(−1.75)</td>
</tr>
<tr>
<td>ACA</td>
<td>−0.117</td>
<td>−0.054</td>
<td>−0.632</td>
<td>−0.199</td>
<td>0.795</td>
<td>1.032</td>
<td>−0.745</td>
</tr>
<tr>
<td>Interaction effects</td>
<td>(−0.34)</td>
<td>(−0.13)</td>
<td>(−1.63)</td>
<td>(−0.38)</td>
<td>(1.02)</td>
<td>(1.98)</td>
<td>(−1.38)</td>
</tr>
</tbody>
</table>

Panel D: Agreement and disagreement between lobby groups i and j

<table>
<thead>
<tr>
<th>Relative influence of lobby group i</th>
<th>Agreement (φ) and disagreement (ψ) between i = IND, AUD</th>
<th>Agreement (φ) and disagreement (ψ) between i = AUD, ACA</th>
<th>Agreement (φ) and disagreement (ψ) between i = ACA, IND</th>
<th>Deviance</th>
<th>ΔDeviance</th>
<th>Fc</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>IND</td>
<td>0.548</td>
<td>0.276</td>
<td>−0.398</td>
<td>2.710</td>
<td>1.510</td>
<td>1.971</td>
<td>0.325</td>
</tr>
<tr>
<td>AUD</td>
<td>(4.29)</td>
<td>(1.09)</td>
<td>(−1.64)</td>
<td>(4.45)</td>
<td>(2.25)</td>
<td>(4.29)</td>
<td>(0.66)</td>
</tr>
<tr>
<td>ACA</td>
<td>−0.103</td>
<td>0.240</td>
<td>−0.753</td>
<td>2.480</td>
<td>1.920</td>
<td>1.749</td>
<td>0.586</td>
</tr>
<tr>
<td>Interaction effects</td>
<td>(0.35)</td>
<td>(0.62)</td>
<td>(−1.99)</td>
<td>(3.16)</td>
<td>(2.87)</td>
<td>(2.95)</td>
<td>(0.01)</td>
</tr>
</tbody>
</table>

| Coefficient estimates are from a log-linear model with a log link function and a Poisson distributed error. The dependent variable is the log of the counts in the cells of Table 1, adjusted for a mean effect. Coefficient estimates are log-odds ratios: a regression coefficient of zero implies odds equal to one, while a positive (negative) coefficient implies odds greater (less) than one. Subscripts IND, AUD and ACA indicate the industry, auditor and academic lobby groups, respectively. Models are described in Table 2.

b The subscripts in parentheses indicate the nested models for which the change in deviance is reported. The deviance for the model of conditional independence (model 1) is 88.981. Note that the θi coefficients in model 1 are also included in all subsequent estimations, but for parsimony are not recorded.

c The F-statistic represents a test of the relative goodness of fit of two nested models. The relative goodness of fit is measured as the difference in the associated deviances (ΔDeviance) of two models, x and y, where x is nested in y. The change in deviance is asymptotically F-distributed. A significant F-statistic indicates that y is a better fitting model than x, or equivalently, that the terms omitted from x are significant.

d The model of agreement and disagreement may be modified to include interaction terms measuring the general odds of success when there is either consensus (ψi) or conflict (ψi). When these interaction terms are included instead of the separate ωi effects for the individual lobby groups, the deviance falls from 88.981 for the model of conditional independence to 63.751 (F = 1.345, p = 0.292). The relevant coefficient estimates are ωi = 0.842 (t = 2.65) and ωi = −0.145 (t = −0.75), again emphasising the positive and significant impact of consensus within the lobbying process.
disagreement with lobbyist $i$. Consistent with the view that agreement among lobby groups represents an important element in the rule-development process, the relative power of industry is seen to have fallen when the empirical model is extended to include interactions with each lobby group, suggesting the existence of important multiplier effects in relation to industry’s perceived influence on the decisions of the legislature. Specifically, the relative odds of industry’s preferred accounting treatment being incorporated into commercial law now declines from approximately 2:1 ($t = 3.27$) in the relative power model to just less than 1:1 ($t = -0.34$) in Model (4.2) in those cases where the only proposal to have been made is from industry. However, the positive and significant coefficient for the $\phi_{\text{IND}} \cdot \phi_{\text{IND}}$ interaction term indicates that the relative odds of an industry-submitted proposal being recognised in commercial law were more than three times greater ($t = 2.55$) when industry’s preferences were aligned with those of one of the remaining lobbying organisations (see Fig. 1). We interpret these findings as evidence that industry’s influence on the decisions of the legislative body was crucially dependent on the support of at least one of the remaining lobby groups.

Several factors may help explain these observed multiplier effects. First, Watts and Zimmerman (1986) argue that industry’s lobbying position is primarily motivated on opportunistic grounds. This self-interest motive can serve to reduce the credibility of industry-submitted proposals, thereby reducing the likelihood of their acceptance. However, to the extent that industry’s position appears more credible when supported by a group of acknowledged financial reporting experts (in this case, either the audit profession or accounting academics), the likelihood of acceptance increases. Secondly, it is widely acknowledged that industry represents a powerful lobby group in Germany. Consequently, for cases in which their position was matched by one or more financial reporting constituencies, a body of opinion may have been created whose political influence was simply too great for the legislature to ignore.

Models (5.1) and (5.2) account for agreement and disagreement between industry and auditors, industry and academics, or auditors and academics. Model (5.1) estimates the main effects for agreement and disagreement between lobbyists $i$ and $j$ and leads to a significant fall in the deviance ($p = 0.019$) with respect to the model of relative influence, as documented in panel D of Table 3, suggesting that identification of the specific parties involved is an important explanatory factor. The findings confirm the inference drawn previously that the auditors were likely to adopt the position of another group, either industry ($t = 4.45$) or academia ($t = 4.29$), while the latter two were more likely to be in conflict with each other ($t = 4.35$). Model (5.2) extends model (5.1) to account for the odds of success in cases of agreement and disagreement between groups $i$ and $j$. Results indicate that industry’s relative power declined substantially when such interactions were accounted for, again suggesting that the ability of German industry to influence the policy decisions of the legislature may have been largely conditional on the support of at least one of the remaining constituent groups. In particular, model (5.2) suggests the existence of a significant multiplier effect when there is agreement between industry and academia.
Thus, while the academic community appears to have exerted relatively little influence over the decisions of the legislature when considered in isolation, German academics are seen to have derived significant influence through their interaction with industry.

6.1. Partitioning by accounting issue

Extant research by Puro (1984) and Sutton (1984) suggests that the distribution of power among alternative lobby groups may vary as a function of the nature of the financial reporting issue under consideration. To explore this possibility further, we partitioned the 169 separate points of accounting law into two groups, one of which comprised all points of law relating to issues of valuation and recognition ($N = 92$) while the other comprised all points of law relating to issues of disclosure and financial statement format ($N = 77$). While acknowledging the inherently arbitrary nature of this partitioning scheme, the approach at least partly captures Sutton’s characterisation of preparers as more concerned with regulations which affect the measurement of earnings and the valuation of assets and liabilities.

$\text{Model Relative influence Agreement and disagreement between } i \text{ and } j$

<table>
<thead>
<tr>
<th>Model</th>
<th>Valuation and recognition</th>
<th>Format and disclosure</th>
<th>Valuation and recognition</th>
<th>Format and disclosure</th>
<th>Valuation and recognition</th>
<th>Format and disclosure</th>
</tr>
</thead>
<tbody>
<tr>
<td>$\omega_{\text{IND}}$</td>
<td>0.251 (1.00)</td>
<td>1.308 (3.68)</td>
<td>0.073 (0.26)</td>
<td>1.206 (3.34)</td>
<td>0.030 (0.07)</td>
<td>0.262 (0.62)</td>
</tr>
<tr>
<td>$\omega_{\text{AUD}}$</td>
<td>0.550 (1.70)</td>
<td>0.000 (0.00)</td>
<td>0.576 (1.61)</td>
<td>0.122 (0.31)</td>
<td>0.486 (0.86)</td>
<td>-0.022 (0.04)</td>
</tr>
<tr>
<td>$\omega_{\text{ACA}}$</td>
<td>-0.133 (-0.45)</td>
<td>-0.898 (-2.51)</td>
<td>-0.234 (-0.72)</td>
<td>-0.72 (-1.86)</td>
<td>-0.859 (-1.51)</td>
<td>-0.730 (-1.41)</td>
</tr>
</tbody>
</table>

Deviance:
- $46.922 (50.431)$
- $16.034 (17.461)$
- $30.888 (32.970)$
- $6.751 (15.787)$

$F$-value:
- $0.566 (2.945)$
- $4.173 (4.091)$
- $0.014 (0.015)$

$p$-value:
- $0.644 (0.003)$
- $0.859 (0.859)$
- $0.571 (0.571)$

$^a$ The initial sample of 169 separate accounting issues has been partitioned into those dealing with valuation and recognition matters ($N = 92$) and those dealing with format and disclosure matters ($N = 77$). Separate generalised linear models were then estimated for each partition. For parsimony, only the relative influence coefficients ($\omega_i$) are reported for all models. The coefficients are from a log-linear model with a log link function and a Poisson distributed error. The dependent variable is the log of the counts from either the valuation and recognition contingency table or format and disclosure contingency table. Coefficient estimates are log-odds ratios: a regression coefficient of zero implies odds equal to one, while a positive (negative) coefficient implies odds greater (less) than one.

Subscripts IND, AUD and ACA indicate the industry, auditor and academic lobby groups, respectively.

$^b$ The subscripts in parentheses indicate the nested models for which the change in deviance is reported. The deviance for the model of conditional independence (Model 1) is 88.981. Note that the $\theta_i$ coefficients in model (1) are also included in all subsequent estimations, but for parsimony are not recorded.

$^c$ The $F$-statistic represents a test of the relative goodness of fit of two nested models. The relative goodness of fit is measured as the difference in the associated deviances ($\Delta D$) of two models, $x$ and $y$, where $x$ is nested in $y$. This difference is asymptotically $F$-distributed. A significant $F$-statistic indicates that $y$ is a better fitting model than $x$, or equivalently, that the terms omitted from $y$ are significant.

$^\dagger$ Partitioning at a finer level of accounting issue was not possible due to an insufficient number of observations in each partition to allow reliable estimation.
quantitatively similar to those reported in Table 3. The relative influence attributable to the industry constituency appears to be restricted to issues of disclosure and financial statement formats: in the case of model (2), industry’s relative log-odds of success are 1.308 ($t = 3.68$) for format and disclosure issues, compared with only 0.251 ($t = 1.00$) for issues of valuation and recognition. However, consistent with the findings presented in Table 3, all $\omega_i$ coefficient estimates in both sample partitions become insignificant when the effects of agreement or disagreement between lobbyists are accounted for, again emphasising the importance of political consensus with respect to the accounting rule-development process. The differential impact of agreement and disagreement on lobbying success across the various financial reporting issues may be inferred from examination of the reductions in the deviance associated with the estimation of model (5.2) for the two sub-samples: the change in deviance is significant for format and disclosure issues ($p = 0.003$) but not for valuation and recognition issues ($p = 0.571$).

7. Summary and conclusions

This paper presents evidence on the impact of constituent lobbying activity on the policy decisions of the German legislature during the transformation of the Fourth Directive into German commercial law. Three main lobby groups are identified: industry, auditors and academics. With the exception of the levels of lobbying activity observed for the academic constituency, the active groups display a remarkable similarity to those documented for the US and similar regulatory regimes. The high level of participation by German accounting academics, relative to the levels observed in the US, can be partially explained by the active market for legal interpretations in Germany. Together, these results support Sutton’s (1984) model of lobbying activity and provide prima facie evidence in support of Sutton’s additional conjecture that these patterns will hold irrespective of the institutional setting.

Using publicly available proposals, we identify the preferences of each lobby group with respect to 169 separate accounting issues. These preferences are then reconciled with the eventual accounting treatment required by the Accounting Directives Law as a means of empirically operationalizing the concepts of power and influence. Several important findings are documented. First, analysis of the main effects models suggests that the industry lobby group exerted the greatest level of relative power over the legislature, while the proposals issued by the academic community display the least likelihood of success. However, when the empirical model is extended to include interaction terms which account for agreement and disagreement between the lobbyists, industry’s relative power is seen to have declined, suggesting that the influence of preparers on the decision of the legislature depended crucially on the support of at least one of the remaining lobby groups. While the academic community on its own appears to have exerted relatively little influence over the decisions of the legislative body, academic experts acting in unison through a formal lobbying group appear to have derived significant influence through their contribution to a process in which agreement between lobbyists was a key feature of accounting lawmaking. Finally, additional tests indicate that industry’s relative power was largely restricted to format and disclosure issues, again depending crucially on the support of either the academic or auditor groups.

Interestingly, German law was amended in May 1998 to mandate a private sector institution to develop accounting standards applicable to group accounts and to advise the Ministry of Justice on changes to accounting law. The Deutscher Standardisierungsrat has since been founded and, once published by the Ministry of Justice, the DSR’s standards should have the standing of legally-recognised accounting principles. The DSR has been modelled on the FASB, and is staffed by independent experts: three from industry, two auditors, one financial analyst and one academic.

---

24 New legislation has also been passed to allow German listed companies the option to use internationally accepted accounting rules in their group accounts as an interim measure until 2004. In turn, the new DSR has been given the task of adapting German accounting principles to international norms by that date.
Although the DSR will instigate due process for the development of its standards, final decisions will require a two-thirds majority of its board. Therefore, in conclusion, we can say that the consensus between the parties which we have demonstrated in this paper is now being institutionalised within the new framework.

Acknowledgements

The authors gratefully acknowledge the helpful suggestions made by Brian Francis, Pelham Gore, Chris Nobes, Ken Peasnell, and workshop participants at Frankfurt University, Lancaster University, the University of Wales, Bangor, the 1997 British Accounting Association Conference, the 1997 European Accounting Association Conference and the 1997 Financial Accounting and Auditing Research Conference. Research assistance was provided by Marc Währisch. Financial assistance was provided by the European Union Human Capital and Mobility Programme, Contract ERBCHRXCT.

References


