

## *Moving targets*

European Accounting Directives

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IASB's SAC member





## *European Accounting Directives*

- ★ **Company Directives – 4<sup>th</sup> (1978) and 7<sup>th</sup> (1983)**
  - banking (1986) and insurance (1991)
- ★ **June 2000 -EU Commission Recommendation**
  - listed companies must prepare IAS consolidated financial statements in 2005
  - Member States may extend requirement to unlisted companies and separate accounts
  - EU endorsement mechanism proposed
    - to oversee integration of IAS in the EU
    - confirm that IAS is an appropriate basis



## *European Accounting Directives*

### ★ **2001 – Proposal - IAS for listed companies**

- in line with recommendation
- endorsement process
  - technical
    - Contact Committee
  - political
    - Accounting Regulatory Committee (ARC)
    - Chaired by the Commission
    - representatives of the Member States
- adopt or reject IAS for application in the EU



## *European Accounting Directives*

### ★ **2001 – Fair value amendments EAD**

- 4<sup>th</sup> and 7<sup>th</sup> directives amended to follow IAS 32 and 39
- Member States must amend their regulations by 2004
  - permit/require fair value valuation of financial instruments
    - in group and separate (option) accounts
  - disclosures regarding all financial instruments
    - market values not evident => disclose underlying assumptions and models
    - disclose fair values per category
    - changes to P&L/equity fair value reserve (AFS 2003, cash flow hedges)



## *European Accounting Directives*

### ★ **2001 – Fair value amendments EAD**

- strategy regarding use of financial instruments
- financial risk management objectives and policies
- policy for hedging forecasted transactions for which hedge accounting is used
- company's exposure to price risk, credit risk, liquidity risk and cash flow risk
- additional disclosures regarding derivatives
  - extent and nature, significant terms and conditions => which may affect amount, timing and certainty of cash flows
  - movements in fair value reserve



## *European Accounting Directives*

### ★ **2001 - EFRAG established**

- private sector - founded by preparers, users, FEE
- proactive contribution to the work of IASB
  - coordinate European standard setters, accounting profession, users, preparers
  - respond to DPs and EDs
- identify issues where IASBs guidance is insufficient
  - recommend changes to IASs, IFRSs/SICs, IFRICs
- initiate changes to EADs if do not conform with IAS
- technical assessment of IASs, IFRSs/SICs, IFRICs
  - recommend acceptance or rejection in the EU



## *European Accounting Directives*

### ★ **June 2002 – The “IAS” regulation**

- does not need to be transposed into national law
- listed companies must apply IAS as endorsed by ARC as of 1 January 2005
- Member States may exempt until 2007
  - listed debt issuers (no equity)
  - listed companies applying US GAAP
- unlisted companies must follow the directives as transposed into national law
- Member States may apply IAS option for unlisted groups and separate accounts
  - realistic after EADs amended 2003



# *Committee of European Securities Regulators (CESR)*

## ★ **2002 Enforcement Standards**

- **No. 1** Enforcement of Standards on Financial Information in Europe
  - 21 high level principles
    - structure of enforcement authority
    - selection of information to be reviewed
    - actions available (incl. public correction)
    - cross-border coordination
    - reporting by enforcement agencies
- **No. 2** Financial Information – Co-ordination of Enforcement Activities (2004)
  - database as a practical reference tool
  - => sets out decisions taken by EU National Enforcers
  - => provides record of previous decisions in particular cases





## *IOSCO – Current sensibilities*

### ★ **EU regulators**

- prepared to accept IFRS financial statements *without* modification/reconciliation

### ★ **US SEC**

- prepared to accept IFRS financial statements from foreign issuers *only with* reconciliation to US GAAP
- no reconciliation for
  - cash flow statement
  - goodwill amortization
  - uniting of interests/acquisitions
  - subsidiaries in hyperinflationary economies
  - proportionate consolidations



## *European Accounting Directives*

### ★ **May 2003 – Amended EADs**

- **complements the IAS regulation**
- removes all inconsistencies between EADs and IFRSs
- Member States may continue using previous options
- Member States can now permit or require all companies to apply IAS as adopted by the EU
  - Member States can follow IASB developments
    - modify the P&L and balance sheet formats
    - require presentation of other statements – cash flow statement or changes in equity
    - permit or require the application of fair value valuations



## *European Accounting Directives*

### ★ **May 2003 – Amended EADs**

– **levels the playing field – current best practice**

– **annual report**

- balanced and comprehensive analysis of development and performance of the business
- financial and non-financial key performance indicators
- information on environmental and employee matters
- description of principal risks and uncertainties

– **audit reports**

- in line with ISA
- scope of audit work
- clearly stated audit opinion – true and fair?
- consistency of annual report and annual accounts



## *European Accounting Directives*

### ★ **May 2003 – New thresholds for SMEs**

- exemptions for SMEs from certain requirements
- if remain below two of the three thresholds

\*the amounts shown are in EUROS

	Small		Medium-sized	
	Old	New	Old	New
Employees	50	50	250	250
Balance sheet total	3 125 000	3 650 000	12 500 000	14 600 000
Net turnover	6 250 000	7 300 000	25 000 000	29 200 000



## *European Accounting Directives*

### ★ **May 2003 - Modernising Company Law and Enhancing Corporate Governance**

★ response to Final Report of High Level Group

#### ★ **transparency proposals related to directors**

- disclosure of remuneration policy of directors' and individual director's remuneration in annual accounts
- prior approval by shareholders meeting of share and share option schemes in which directors participate
- recognition of costs of share option schemes in profit and loss accounts (not just in notes to the accounts)

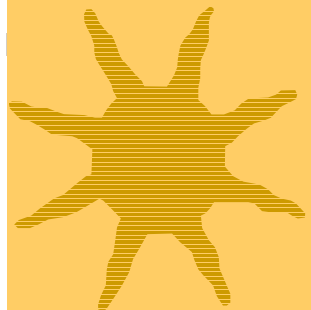
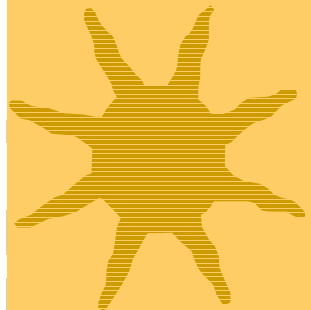
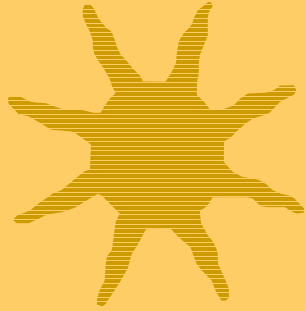


## *European Accounting Directives*

### ★ **May 2003 - Modernising Company Law and Enhancing Corporate Governance**

#### ★ **proposals to modernise capital regimes**

- introduction of "real" no par value shares (i.e. shares without any reference to nominal or fractional value)
- limiting need for expert valuations of contributions in kind
- partial relaxation of prohibition of financial assistance for acquisition of shares by third parties
- introduction of right to acquire own shares up to the limits of distributable reserves
- introduction of squeeze-out and sell-out rights
- dividends based on solvency



## *Moving targets*

IASB and IFRSs

Rita Ilisson

IASB's SAC member





## *From IASC to IASB*

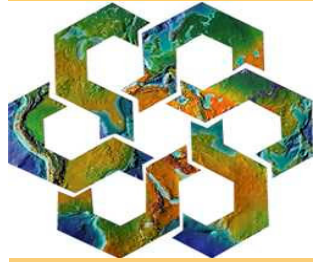
Old (1973 to 2000)

- ★ International Accounting Standards *Committee*
- ★ International *Accounting* Standards (IAS)

New (2001 onwards)

- ★ International Accounting Standards *Board* (IASB)
- ★ International *Financial Reporting* Standards (IFRS)
- ★ IFRS encompasses:
  - IFRS
  - IFRIC interpretations
  - IAS
  - SIC





## *From IASC to IASB*

### **IASC Board**

- ★ volunteers, constituencies
- ★ approve *IAS*

### **Standards Interpretations Committee (SIC) Consultative Group**

- ★ advise Board

### **Advisory Council**

- ★ oversight
- ★ funding

### **IASB Board**

- ★ *full-time, independent*
- ★ approve *IFRS*
- ★ *national liaisons*

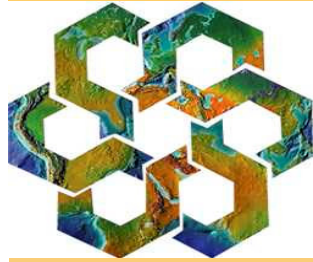
### **IFRIC**

### **Standards Advisory Council**

- ★ advise Board

### **Trustees**

- ★ *appoint Board, SAC...*
- ★ oversight
- ★ funding



## *IASB Objectives (2001 onwards)*

- *single set* of high quality, understandable and enforceable *global accounting standards*
- *transparent* and *comparable* information in general purpose financial statements
- *promote use of /rigorous application*
- *co-operation with national standard setters* to achieve *convergence* of accounting standards

IFRS and US GAAP convergence - short-term projects

=>reconcilable differences



## *The new IASB*

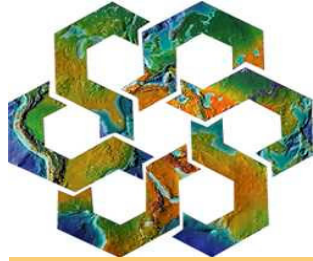
### ★ **international acceptance ?**

- compromises vs high quality standards ?
- comparability/prescriptiveness ?
- eradicate alternatives and inconsistencies ?
- framework approach ?
- quality, ease of use and enforceability ?
- level playing field vis-a-vis US GAAP ?

### ★ **convergence ?**

- comparable accounting for comparable transactions
- common conceptual framework
- eradicating alternative treatments





## *Reprioritisation of Initial Agenda*



### ★ I. Leadership and Convergence

- **Accounting for Insurance Contracts**
  - phase 1 - **IFRS Q1 04** (sequence)
  - phase 2 – ED Q? 0?
- **Business Combinations**
  - phase 1 – **IFRS Q1 04** (sequence)
  - phase 2 - ED Q3 03, IFRS after 2005
- **Performance Reporting**
  - ED Q4 03
- **Accounting for Share-Based Payments**
  - **IFRS Q1 04**

# *Reprioritisation of Initial Agenda*



- **II. Easier application of IFRSs**
  - **Guidance on First-Time Adoption**
    - IFRS 1 2Q 03
  - **Financial risk and other amendments to financial instruments disclosures**
    - ED Q2 2004 => Financial disclosures ED
- **III. Improvements**
  - **Improvements to existing IAS**
    - IFRS Q4 03
  - **Improvements to IAS 32 and 39**
    - IFRS Q4 03 (sequence)

## *IMP – Improvements project*

- ★ IAS 1 Presentation of Financial Statements
- ★ IAS 2 Inventories
- ★ IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors
- ★ IAS 10 Events After the Balance Sheet Date
- ★ IAS 16 Property, Plant and Equipment
- ★ IAS 17 Leases
- ★ IAS 18 The Effects of Changes in Foreign Exchange Rates
- ★ IAS 24 Related Party Disclosures
- ★ IAS 27 Consolidated and Separate Financial Statements
- ★ IAS 28 Investments in Associates
- ★ IAS 31 Interest in Joint Ventures
- ★ IAS 33 Earnings per Share
- ★ IAS 40 Investment Property

# *IMP – Improvements project*

## ★ **IAS 1 Presentation of Financial Statements**

- unreserved declaration of compliance with IFRS (IAS as endorsed by the EU)
- “true and fair” instead of “present fairly”
- ✂ extraordinary items
- ✂ minority interest => between liabilities and equity
- ✂ minority interests’ share of group profit or loss
  - => neither revenue nor expense
  - ✓ minority interests’ share of group profit or loss =>
    - allocation of group net income (profit/loss)
    - majority’s share
    - minority’s share
- disclosures
  - key judgements and assumptions

# *IMP – Improvements project*

## ★ IAS 2 Inventories

- ✂ “historical cost system” and “matching principle”
- ✂ LIFO
- measurement => lower of cost or net realisable value
- ▲ scoped out => construction contracts, financial instruments, biological assets at point of harvest
- ▲ scoped out => measurement
  - producers of agricultural/forest products, minerals/mineral products
    - net realisable value – industry practice
  - commodity brokers/traders
    - fair value less costs to sell
- disclosures
  - expensed amount
  - write-down and reversal
  - amount at fair value less costs to sell



# *IMP – Improvements project*

## **★ IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors**

- accounting policies IAS 1 => IAS 8
- net profit/loss IAS 8 => IAS 1
  - no definition for operating income
  - goodwill ? impairment of PPE ?
- required change in accounting policy under IFRS
  - transitional requirements
- voluntary change in accounting policy
  - retrospective restatement
- all (material) errors
  - retrospective restatement

## *IMP – Improvements project*

### ★ **IAS 10 Events After the Balance Sheet Date**

- dividends declared after BS date => not a liability or adjusting event
- liability – if payment cannot be deferred more than 12 mths on BS date => current

### ★ **IAS 16 Property, Plant and Equipment**

- subsequent costs => if economic benefits enhanced compared with pre-investment state
- cost = asset dismantlements, removal and restoration (previously only installation costs)
  - => these costs may give rise to a provision
- asset exchanges => at fair values unless transaction lacks commercial substance
  - previously => acquired asset at fair value unless similar

# *Reprioritisation of Initial Agenda*



## ★ **Active research topics**

- SMEs
- accounting for leases
- accounting concepts
- aspects of accounting for financial instruments

## ★ **Other topics**

- accounting for extractive industries
- definitions of elements of financial statements
- derecognition issues other than those in IAS 39
- impairment of assets
- liabilities
- MD&A