IMF COMMITTEE ON BALANCE OF PAYMENTS STATISTICS AND OECD WORKSHOP ON INTERNATIONAL INVESTMENT STATISTICS

DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG)

BACKGROUND PAPER (DITEG) #1

INTERNATIONAL ACCOUNTING STANDARDS AND VALUATION OF DIRECT INVESTMENT EQUITY STOCKS

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October 2004

Introduction

1. In its June 2004 meeting, DITEG held a discussion on different valuation methods for foreign direct investment (equity) stocks in non-quoted shares. Particular attention was paid to the method applied in the European Union, the so-called "own funds at book value" method (hereinafter OFBV).

2. The OFBV method aims at getting the value of the target direct investment company (DIC) through the selection of a limited number of DIC's balance sheet items. In particular, the following components of the (unlisted) DIC's balance sheet should be considered:[1]

i) Nominal (paid-up) capital excluding own shares;

ii) All types of reserves including shares premium accounts and investment grants; and

iii) Non-distributed profits net of losses (including results for the current year).

3. Since the own funds of a company represent its net worth, i.e. the arithmetical difference between assets and liabilities,[2] the valuation methods employed to record assets and liabilities in the balance sheet of the DIC are crucial to determine how close the final result might be to the (hypothetical) market value of the company.[3]

4. For this reason, the shift from current accounting rules (in many cases purely ruled at the national level) toward a single set of international accounting standards (IAS) and the evolution of the latter towards fair valuation of financial and non-financial assets and liabilities are key to determine how close the results might be to the ultimate target of getting an approximation to the market value of unlisted DIC.

5. The first section of this document summarises the state of play of discussions concerning the process of approval of the new IAS. The second section further elaborates on the scope of application of the IAS across different sectors and countries. The third section explores the consequences of the new IAS on the valuation of non-quoted shares based on OFBV and the plans of the ECB as regards valuation methods for the euro area international investment position (i.i.p.). The fourth section concludes and puts forward some proposals to be considered by DITEG members.

I State of play of the process of approval of IAS: IAS 32 and 39

6. The International Accounting Standards Board (IASB) is the body in charge of developing IAS. The IASB is an independent, privately funded accounting setter based in London, which has the support of governments of major economies. The IASB has a mandate to create a single set of high-quality, enforceable global accounting rules for use by the world's capital markets and requires global recognition of its Standards. The new accounting standards that the IASB will develop will be called International

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1 For a more exhaustive description of individual components of OFBV see the background document "*Valuation of FDI stocks remaining conceptual issues of the 'Own funds at book value' method*" distributed to the DITEG in June 2004.

2 Assuming a positive result; otherwise, the value should be zero.

3 Intangibles not recorded on-balance such as "goodwill" are excluded from this valuation method.

Financial Reporting Standards (IFRSs). For the purpose of this note, the terms IAS and IFRS are used indistinguishably.

7. In total, there are at present 34 IAS[4], 31 related interpretations (SICs) and 5 international Financial Reporting Standards (IFRS). The European Commission will formally enforce listed companies in the European Union to use IAS for annual consolidated accounts as of January 2005 onwards.[5]

8. From the statistical viewpoint and considering the close links between accounting data and statistical reports, [6] the implementation of IAS is a welcome development as it will extend the application of market/fair value to securities portfolios and to positions in financial derivatives. This is broadly consistent with international statistical standards (SNA93/ESA95 and BPM5) and with the ECB statistical requirements. Having said this, the application of fair values to some specific instruments - more specifically to loans/deposits - could hamper the provision of nominal values, which users deem necessary for monetary and financial stability analyses.

9. More specifically, at the current juncture the most important difficulties lie on IAS 32 and IAS 39. These standards cover the types of financial instruments to be disclosed on the balance sheet (IAS32) and the recognition and measurement/valuation (IAS 39). These two standards have been subject to several rounds of public exposure for comments. IAS 39 is being partially revised concerning the so-called fair value option (FVO) which has been subject to public comments since April 2004 through an Exposure Draft.[7]

10. The main concerns towards IAS 39 have been expressed by the BIS "Basel Committee", prudential supervisors and the ECB. In response to these concerns, the April 2004 Exposure Draft limited the application of the FVO to (i) financial assets and liabilities for which the fair value is verifiable; and to (ii) five categories of financial assets and liabilities. [8] The move towards fair value is reinforced by new disclosure requirements (in IAS 32 and in the Exposure Draft 7 on financial instruments disclosure).

11. Given the technical complexity of the issues at stake and the difficulty of reaching a consensual solution among all parties concerned in time before the stipulated deadline for endorsement, it was considered that (part of) IAS 39 would not apply together with the other standards.

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4 The European Union Commission has already endorsed 32 of them.

5 The EU will soon reach the final stage of implementing the financial reporting strategy which was unanimously agreed under the Lisbon Agenda in June 2000. According to Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards, from 1 January 2005, more than 7000 listed European companies will have to prepare their consolidated accounts according to the International Accounting Standards (IAS), as endorsed by the Commission.

6 Please refer to La Liberté (2003).

7 The (to date) last Exposure Draft on IAS 39 was issued in July 2004.

8 Namely (i) items with one or more embedded derivatives; (ii) financial liabilities with a contractual link to the performance of assets which are at fair value; (iii) items for which the exposure to changes in the fair value of the financial asset or financial liability is substantially offset by the exposure to the changes in the fair value of another financial asset or financial liability, including a derivative; (iv) financial assets other than loans and receivables and (v) items that other Standards allow or require to be designated as at fair value through profit or loss. This is a complement to the obligation of recording all derivatives at market value in order to permit consistent valuation rules for hedging.

12. With a view to permitting the partial application of IAS 39 as of January 2005, in September 2004 the European Commission proposed to adopt IAS 39 while carving out the application of fair valuation for financial liabilities and other provisions concerning hedging of interest rate risk. This proposal was endorsed by the Accounting and Regulatory Committee (ARC) at its meeting on 1 October 2004. Within the next few weeks, the IAS 39 will become law in Europe, by means of a European Commission Regulation.

13. The European Commission considers that, at the current juncture, a limited carve out of certain provisions was as close as possible to the objective of a full application of IAS from 1 January 2005 onwards, while the deferral of the adoption of IAS 39 would be a major setback which could cause market confusion. The ultimate goal will still be the adoption in full of IAS 39; the European Commission has actually made it clear that the carve out should be temporary and that the issue is expected to be resolved in the course of 2005.

14. According to the European Commission, the final endorsement of a revised version of IAS 39 could occur as early as mid 2005, assuming it finds a compromise amongst stakeholders to expand the FVO to financial liabilities whilst at the same time restricting the scope of the option itself . Until that point in time, the version of IAS 39 which will become mandatory in January 2005 in the EU permits companies to report any financial assets (<u>including non-negotiable instruments and loans</u>) at fair value, while liabilities (excluding financial derivatives) can only be valued at nominal value (unless they are held for trading). [9]

II Scope of application of IAS across sectors and EU countries

15. The previous section described some foreseeable benefits for statistics which may derive from the introduction of IAS, in terms not only of valuation principles, but also of further consistency in the accounting rules applied across countries.

16. In this regard, one additional factor to be borne in mind is the extent to which IAS will be used across different types of companies and the decisions that could eventually be adopted by EU countries. This Section only deals with the situation in the EU countries. It is expected that countries outside the EU may also adopt IAS. The incorporation of other experiences outside the EU and the specific features of accounting standards in other countries could be a very useful complement to this paper.

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[9] Several parties are criticizing the endorsement in Europe of an amended version of IAS 39 as the current compromise puts at risk the comparability of companies' financial statements as well as the efforts to converge international and US accounting standards.

17. In principle, in the European Union IAS will only be mandatory for consolidated accounts of listed companies. The possibility to amplify the scope to other types of companies (unlisted) and accounts (individual/non-consolidated accounts) is being decided by each EU Member State. [10]

18. The flexibility that the IAS Regulation provides to EU Member States to apply IAS to individual accounts and to unlisted companies may be disruptive for statistics. The possibility that listed companies in the EU can be permitted or required to apply the IAS in their individual accounts while unlisted companies may be permitted or required to maintain the historical cost accounting framework could be an important distorting factor for statistics compilers. Differences in the approaches taken by Member States and in the timing of implementation at the national level may eventually affect the quality of EU/euro area statistics.

19. Many countries have already taken a decision as to whether or not they will require/permit the application of IAS to unlisted companies. Annex 1 presents a detailed description of the individual decisions taken by EU MS. Table 1 below is a summary of the decisions taken by EU countries. A majority of them have decided or will likely decide to amplify the scope of application of the new IAS to all types of companies, either permitting or imposing the application of IAS beyond what is required by European law.

Table 1 Expected scope of application of IAS *(as at July 2004)*

Type of company	Option	Consolidated accounts only	Individual accounts
Listed	Require	ES, FR(*), AT, LV	GR, BE(**), IT, FI, PT, CZ, HU, EE, CY, LT, SI, SK
	Permit		DE, DK, UK, NL, LU(***), IE(***), SE, PL
Unlisted	Require	SK	IT, EE, CY, LT(****), SI
	Permit	AT, FR(*), CZ, ES	BE(**), DE, GR, FI, PT, DK, HU, UK, NL, SE, LU(***), IE(***), PL

(*) Tax and legal questions should be resolved before further extension of IAS to non-listed companies may be decided.
(**) For information of investors only.
(***) Most likely option. Not yet fully decided.
(****) Only banks

Source: European Commission, DG-Internal Market accounting website

[10] In this respect, the EU Council adopted in May 2003 the so-called "Modernisation Directive" which allows Member States which do not apply IAS to all companies to move towards similar financial reporting. In particular, the Directive introduces greater flexibility with regard to presentation of balance sheets and profit and loss accounts (introduction of an option for Member States to permit or require a classification of balance sheet and profit and loss items by their nature and/or by degree of liquidity) as well as the possibility to permit or require revaluation and the use of fair value accounting.

III Impact of the IAS on the valuation of FDI equity stocks based on OFBV

20. While the introduction of a set of harmonised accounting standards in the EU will imply a closer approximation to market/fair values for financial assets and liabilities besides the already mentioned benefits in terms of further harmonisation, some shortcomings should also be borne in mind.

21. As mentioned in the previous sections, there is a certain scope for uncertainty as to the final scope of the so-called fair value option of IAS 39.[11] Additionally, though most countries have already expressed their willingness to either permit or require that *all* types of companies apply IAS, there is still a certain level of uncertainty as to the possible co-existence of heterogeneous accounting rules across different types of reporters and across countries.

22. The final resolution of the former two points may somewhat affect the proximity of the valuation based on OFBV to an estimated market value for DIC. In any case, the ECB plans to compare on a regular basis the results of the OFBV at an aggregate level (i.e. for inward and outward FDI of the euro area) with other market estimates.

23. Concerning the plans for the euro area international investment position, and with regard to whether some market estimates may be compiled at some stage, for the time being there are plans to start compiling them at an aggregate level in the form of memorandum items.

24. In particular, as of end-year positions corresponding to 2005[12], the euro area i.i.p. will show supplementary items with an estimate of FDI stocks in unquoted shares based on the projection of a ratio capitalisation (i.e. stock-exchange quotation) to OFBV from listed to non-listed FDI companies. Such estimates will only be calculated at an aggregate level, i.e. for inward and outward euro area FDI, with no further details by counterpart country.

25. The main reason why not more detailed figures (i.e. market estimates of FDI in non-listed companies/non-quoted shares by counterpart country) will be compiled is the expected lack of representativeness of listed companies for a significant number of specific counterpart countries, both inside –for inward FDI– and outside –for outward FDI– the euro area.

26. The ECB understands that such problems are equally applicable worldwide. Similar shortcomings most likely apply also to the compilation of market estimates for non-quoted shares at the level of specific sectors of activity.

IV Conclusions and proposals

27. This paper has reviewed the current state of play of the process of approval of the new IAS, the decisions of EU Member States concerning the application of IAS to non-listed companies and the consequences for the valuation of FDI equity stocks based on OFBV.

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[11] There are, in particular, prudential reasons to exclude from fair valuation loans and deposits, as highlighted, inter alia, by the Basel Committee.

[12] Back series will also cover the year 2004.

28. Additionally, the paper presented the view that to compile FDI statistics at the level of counterpart countries and sector of activity of investors/investees, information need to be collected from the balance sheet of non-listed DIC.

29. The forthcoming discussions related to the possibility of establishing a Co-ordinated Direct Investment Survey (CDIS) may give the opportunity to consider some relevant aspects in a forward looking manner.

30. Some of the problems this paper tries to anticipate are related to, on the one hand, the need to distinguish between instruments which are fundamentally different within (direct investment) equity and, on the other hand, the need to ensure a certain level of comparability as regards the FDI statistics compiled by different economies.

31. Against this background, two proposals are put forward to DITEG:

(a) ***Introduce a split between quoted and unquoted shares in FDI equity*** both in the b.o.p. and the i.i.p. standard components. This proposal would present manifold advantages: in addition to establishing a clear borderline between two instruments which are fundamentally different in nature, it would approximate further the disclosure of b.o.p./i.i.p items to national accounts standards, since the split between quoted and unquoted shares is explicitly covered in both SNA93 and ESA95.

(b) ***Promote the compilation of detailed series by counterpart country*** (origin/destination of direct investment) ***and by sector of activity*** (investor/investee companies) of FDI equity stocks ***based on a single definition of OFBV***. Since such a single definition would represent a symmetric measure of FDI equity stocks from the perspective of both investor sector/country and investee sector/country, the proposal would establish a means to enhance international comparability by enabling a centralised exchange of information amongst countries through a central platform like the IMF project for a CDIS.

Points for Discussion

1) ***Do DITEG members consider that the impact of IAS on the valuation of FDI equity stocks based on OFBV should be seen as a welcome development? Do DITEG members agree with the need to monitor possible difficulties derived from different decisions and different path of adoption of IAS across countries? Do DITEG members agree to gather information on the actual implementation of IAS outside the EU?***

2) ***Do DITEG members agree with the proposal to split direct investment in equity into quoted and unquoted shares on both analytical and practical grounds?***

3) ***Do DITEG members agree with the proposal to compile detailed series by counterpart country (origin/destination of direct investment) and by sector of activity (investor/investee companies) of FDI equity stocks based on a single definition of OFBV for the purpose of exchanging information across countries?***

References

- CMFB opinion on the Fair Value Option under IAS 39 (http://www.iasb.org/docs/ed-ias39fv/IAS39_FairValue_CL15.pdf)
- European Commission/Internal Market/Accounting website (http://europa.eu.int/comm/internal_market/accounting/index_en.htm)
- Eurostat/ECB Accounting and Statistics Task Force (http://forum.europa.eu.int/irc/dsis/accstat/info/data/en/)
- International Accounting Standards Board website (http://www.iasb.org/index.asp)
- Lucie Laliberté (2003) "*The relationship between international accounting standards and statistical standards*", presented in the July 2003 thematic meeting of the Statistics Committee of the European System of Central Banks.
- Revue d'économie financière n°71 (2 - 2003); "Juste valeur et évaluation des actifs"; ed. Association d`économie financière (www.aef.asso.fr)
- Statistics Committee (July 2004) *"Impact of International Accounting Standards on Money and Banking statistics" (unpublished)*
- Statistics Committee (September 2003) *"Impact of International Accounting Standards on External Statistics" (unpublished)*
- Task Force on Foreign Direct Investment "*Final report of the Task Force on Foreign Direct Investment (chapter 3)*", published on the ECB website (http://www.ecb.int/pub/pdf/other/foreigndirectinvestment200403en.pdf)

Annex 1: plans for implementation of IAS in European countries (Source: European Commission website)

Planned Implementation of the IAS Regulation (1606/2002) in the EU and EEA (Published for information purposes only) **Date 12/07/04** **1/2**

European Commission	Austria	Belgium	Denmark	Finland	France	Germany	Greece	Italy	Ireland
Status of the implementation of IAS	Proposal	Proposal	Proposal[1]	Proposal	Proposal	Proposal	Final law	Final law	Consultation[2]
Article 5(a) of the IAS Regulation **LISTED COMPANIES** 1. Will your MS use the option to **permit** IAS in the **annual accounts** for listed companies?	No	See footnote[3]	Until 2009: Yes After 2009: No	Yes	Not until tax and legal questions are settled	Yes[4]	No	No	Probably yes
2. Will your MS use the option to **require** IAS in the **annual accounts** for listed companies?	No	See footnote[3]	Until 2009: No After 2009: Yes	No	No	No	Yes	Yes[5], except for insurance	No
Article 5(b) of the IAS Regulation **OTHER COMPANIES** 1. Will your MS use the option to **permit** IAS in the **consolidated accounts** for other companies? If yes, what type of companies?	Yes, all companies	Yes, probably all types	Yes, all types	Yes[6], all types	Yes, consolidated companies	Yes, all types	Yes[6]	Yes, except for small enterprises	Yes, probably all types
2. Will your MS use the option to **require** IAS in the **consolidated accounts** for other companies? If yes, what type of companies?	No	Possibly for credit institutions Probably in the future for other companies	No	No	No	Yes, companies, which have filed for a listing	No	Yes, some companies[7]	No
3. Will your MS use the option to **permit** IAS in the **annual accounts** for other companies? If yes, what type of companies?	No	See footnote[3]	Yes, all types	Yes[6], All types[8]	No	Yes[4] All types	Yes[6]	Yes, except for insurance, small enterprises and required companies	Yes, probably all types
4. Will your MS use the option to **require** IAS in the **annual accounts** for other companies? If yes, what type of companies?	No	See footnote[3]	No	No	No	No	No	Yes, some companies[9]	No
Article 9 of the IAS Regulation **(a)** Will your MS use the option to **defer** the application of IAS **until 2007** for companies whose debt securities only are admitted on a regulated market of any MS?	Probably yes	Probably yes	Yes	Yes	Yes, possibly	Yes	No	No	No
(b) Will your MS use the option to **defer** the application of IAS **until 2007** for companies whose securities are admitted to public trading in a non-member State and which, for that purpose, have been using internationally accepted standards since a financial year that started prior to the publication of the IAS Regulation in the OJ?	Probably yes	Probably yes	No	No	No	Yes	No	No	No
Miscellaneous Is earlier adoption (before 2005) of IAS allowed? If yes, for what type of companies/ from when?	Yes, cons. accounts since 1998	Yes, cons. accounts for all companies	Yes, when a full set of IASs are adopted	1. Listed cos: cons. accounts 30.9.2003 2. Other cos (not ins. cos): all accounts 2004	No	Yes, option for listed companies (as from 1998)	31.12.2004 Yes[6]	No	No

[1] Denmark: Proposal pending in Parliament. Covers all enterprises except financial companies/institutions. As regards financial entities it is foreseen that they will be neither permitted nor required to use IAS.
[2] Ireland: The information given is only indicative and might still change after completion of the consultation process
[3] Belgium: To be examined with tax and legal aspects
[4] Germany: For purposes of information only. Financial statements that are in line with national accounting law will continue to be required for purposes of profit distribution, taxation and financial services supervision
[5] Italy: Listed insurance enterprises must comply with IAS only if they do not draw up consolidated accounts
[6] Finland and Greece: Companies, which are audited by certified auditors
[7] Italy: Supervised financial companies; companies with financial instruments widely distributed among the public; insurance companies.
[8] Finland: Application of national law will be mandatory for insurance companies in annual accounts for a transition period
[9] Italy: Supervised financial companies; companies with financial instruments widely distributed among the public

European Commission	Luxemburg	Netherlands	Portugal	Spain	Sweden	UK	Norway	Iceland	Lichtenstein
Status of the implementation of IAS	Work group	Consultation	Work Group[10]	Final law	Proposal	Consultation	Consultation	Work group	Final law
Article 5(a) of the IAS Regulation **LISTED COMPANIES** 1. Will your MS use the option to **permit** IAS in the **annual accounts** for listed companies?	Yes, possibly 2007 if tax solution	Yes	No	No	Yes	Yes	Probably no	Yes	Yes
2. Will your MS use the option to **require** IAS in the **annual accounts** for listed companies?	Probably no	No	Yes	No	No	No	No	Probably no	No

European Commission	Luxemburg	Netherlands	Portugal	Spain	Sweden	UK	Norway	Iceland	Lichtenstein
Article 5(b) of the IAS Regulation **OTHER COMPANIES** 1. Will your MS use the option to **permit** IAS in the **consolidated accounts** for other companies? If yes, what type of companies?	Yes, banks 2003	Yes, all types	Yes, companies with certified accounts	Yes, all types	Yes, all types	Yes, all types of companies except for the charity sector	Probably yes. All types	Yes, all types	Yes, all types
2. Will your MS use the option to **require** IAS in the **consolidated accounts** for other companies? If yes, what type of companies?	Probably no	No	No	No	Possibly for the financial sector[11]	No	No	No	No
3. Will your MS use the option to **permit** IAS in the **annual accounts** for other companies? If yes, what type of companies?	Yes possibly 2007 if tax solution	Yes, all types	Yes, companies with certified accounts	No	Yes, all types	Yes, all types of companies except for the charity sector	Probably no	Yes, all types	Yes, all types
4. Will your MS use the option to **require** IAS in the **annual accounts** for other companies? If yes, what type of companies?	Probably no	No	No	No	No	No	No	No	No

European Commission	Luxemburg	Netherlands	Portugal	Spain	Sweden	UK	Norway	Iceland	Lichtenstein
Article 9 of the IAS Regulation (a) Will your MS use the option to **defer** the application of IAS **until 2007** for companies whose debt securities only are admitted on a regulated market of any MS?	Probably yes	No	No	Yes, except for banking sector companies	Yes	No	Yes	Probably yes	No
(b) Will your MS use the option to **defer** the application of IAS **until 2007** for companies whose securities are admitted to public trading in a non-member State and which, for that purpose, have been using internationally accepted standards since a financial year that started prior to the publication of the IAS Regulation in the OJ?	No decision yet	No	No	No	No	No	Yes	Probably yes	No

European Commission	Luxemburg	Netherlands	Portugal	Spain	Sweden	UK	Norway	Iceland	Lichtenstein
Miscellaneous Is earlier adoption (before 2005) of IAS allowed? If yes, for what type of companies/ from when?	Derogations on an individual basis	No	No	No	No	No	No, but nearly possible within national rules	Probably yes	31.12.2002 Yes, all types

[10] Portugal: Proposal submitted by CNC to Government. Does not include the position of the banking and insurance sector
[11] Sweden: A requirement for financial institutions and insurance companies to apply IAS would earliest enter into force 2006.

Planned Implementation of the IAS Regulation (1606/2002) in the new Member States **(Published for information purposes only)** **Date: 22/07/04**

European Commission	Czech Rep.	Cyprus	Estonia	Hungary	Latvia	Lithuania	Malta	Poland	Slovakia	Slovenia
Status of the implementation of IAS	Final law		Final law	Final law	Final law[1]	Final law		Proposal[2]	Final law	Proposal
Article 5(a) of the IAS Regulation **LISTED COMPANIES** 1. Will your MS use the option to **permit** IAS in the **annual accounts** for listed companies?	No		No	No[3]	No[4]	No		Yes	No	No
2. Will your MS use the option to **require** IAS in the **annual accounts** for listed companies?	Yes		Yes	No	No	Yes		No	Yes	Yes
Article 5(b) of the IAS Regulation **OTHER COMPANIES** 1. Will your MS use the option to **permit** IAS in the **consolidated accounts** for other companies? If yes, what type of companies?	Yes All types of companies		Yes All types	Yes, all types of companies within the scope of Act of Accounting	No[3]	No		Yes, 1) companies having filed for admission to public trading; 2) any parent comp. being a subs. of another parent u/t preparing its cons. acc. in line with IAS	Yes	Yes, all types of companies which decide to use IASs for at least 5 years
2. Will your MS use the option to **require** IAS in the **consolidated accounts** for other companies? If yes, what type of companies?	No		Yes, credit and other financial institutions	No	No	Yes, for banks		Yes, banks	Yes, all types.[5]	Yes, for banks and insurance companies
3. Will your MS use the option to **permit** IAS in the **annual accounts** for other companies? If yes, what type of companies?	No		Yes All types	No[6]	No[3]	No		Yes, 1) companies having filed for admission to public trading; 2) companies whose parent u/t prepares its cons. acc. in line with IAS	No	Yes, all types of companies which decide to use IASs for at least 5 years
4. Will your MS use the option to **require** IAS in the **annual accounts** for other companies? If yes, what type of companies?	No		Yes, credit and other financial institutions	No	No	Yes, for banks		No	No	Yes, for banks and insurance companies
Article 9 of the IAS Regulation (a) Will your MS use the option to **defer** the application of IAS **until 2007** for companies whose debt securities only are admitted on a regulated market of any MS?	No		No	Issue under consideration	No	No		Yes	No	No
(b) Will your MS use the option to **defer** the application of IAS **until 2007** for companies whose securities are admitted to public trading in a non-member State and which, for that purpose, have been using internationally accepted standards since a financial year that started prior to the publication of the IAS Regulation in the OJ?	No		No	Issue under consideration	No	No		No	No	No
Miscellaneous Is earlier adoption (before 2005) of IAS allowed? If yes, for what type of companies/ from when?	Yes[7]		Yes All types 01.01.2003	No[5]	No[3]	Yes, for banks since 1997		No	Yes, listed companies since 01.01.2004	No

[1] Latvia: Legislation currently in force. Covers all enterprises except financial and capital market participants (banks, insurers, etc)
[2] Poland: Proposal pending in the Parliament
[3] Hungary: The application of IAS for informal purposes is permitted, and the listing rules are in some cases requires the application of IAS. Nevertheless the companies are obliged to prepare annual accounts according to the Accounting Act. Changing of position is not anticipated until the tax and legal issues are not solved.
[4] Latvia: Companies can use IAS in the annual and consolidated accounts as so far as it is not in conflict with national accounting laws.
[5] Slovakia: Application of IAS for preparing consolidated accounts for all companies (listed and non- listed) from the year 2005.
[6] Hungary: It is permitted to apply IASs for informal purposes; however the companies are obliged to prepare annual accounts according to the Accounting Act. It is not anticipated to change the position before the tax and legal issues are solved.
[7] Czech Rep.: Yes, effective from the first accounting period following after Accession Treaty come into force, for companies mentioned above

Annex 2: specific details on the contents of IAS 32 and 39

(c) **IAS 32 "*Financial instruments: disclosure and presentation*".** Prescribes approaches for the disclosure of on-balance sheet and off-balance sheet financial instruments in respect of the company's financial position, performance and cash flows.

(d) **IAS 39 *"Financial instruments: Recognition and measurement".*** Prescribes approaches for the recognition and valuation of financial assets and liabilities: all financial assets and liabilities are recognised on-balance sheet, including derivatives.

Definitions

(e) Four categories of assets/liabilities are established:

Held for trading: financial assets and liabilities that are (i) acquired or incurred principally for the purpose of selling or repurchasing it in the near term; (ii) part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking; or (iii) a derivative (except for a derivative that is a designated and effective hedging instrument).

Held-to-maturity: investments that are non-derivative financial assets with fixed or determinable payments and fixed maturity that an entity has the positive intention and ability to hold to maturity other than: (a) those that the entity upon initial recognition designates as at fair value through profit or loss; (b) those that the entity designates as available for sale; and (c) those that meet the definition of loans and receivables.

Loans and receivables: non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than: (a) those that the entity intends to sell immediately or in the near term, which shall be classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; (b) those that the entity upon initial recognition designates as available for sale; or (c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which shall be classified as available for sale.

Available for sale: non-derivative financial assets that are none of the above.

Measurement (valuation)

(f) All financial assets are measured at fair value, except for unquoted shares, securities held to maturity and loans and receivables originated by the enterprise and not held for trading.

(g) After acquisition, most financial liabilities are measured at original recorded amount less principle repayments and amortisation. Only derivatives and liabilities held for trading (such as borrowed securities) are re-measured to fair value.

(h) For those financial assets and liabilities that are re-measured to fair value, an enterprise will recognise in net profit only those changes in fair value relating to financial assets and liabilities it has sold, at which point the realised gain or loss is reported in net profit or loss. For this purpose, derivatives are always deemed to be held for trading unless they are designated as hedging instruments.

Impairment and uncollectability of financial assets

(i) A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one of more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Hedge accounting

(j) If there is a designated hedging relationship between a hedging instrument and a hedged item, accounting for the gain or loss on the hedging instrument and the hedged item shall be recognised in the P&L account. Hedging relationships are of three types: (a) fair value hedge: a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect profit or loss. (b) cash flow hedge: a hedge of the exposure to variability in cash flows that (i) is attributable to a particular risk associated with a recognised asset or liability (such as all or some future interest payments on variable rate debt) or a highly probable forecast transaction and (ii) could affect profit or loss. (c) hedge of a net investment in a foreign operation as defined in IAS 21. A hedging relationship qualifies for hedge accounting under if, and only if, all of the following conditions are met: (a) At the inception of the hedge there is formal designation and documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge. (b) The hedge is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship. (c) For cash flow hedges, a forecast transaction that is the subject of the hedge must be highly probable and must present an exposure to variations in cash flows that could ultimately affect profit or loss. (d) The effectiveness of the hedge can be reliably measured, ie the fair value or cash flows of the hedged item that are attributable to the hedged risk and the fair value of the hedging instrument can be reliably measured. e) The hedge is assessed on an ongoing basis and determined actually to have been highly effective throughout the financial reporting periods for which the hedge was designated.

Annex 3

IAS: stable platform and EU status[13]

Standard	Title	Status in the EU
-	Framework (This general reference framework is not a standard and applies only in the absence of any specific standard)	It was **not incorporated in the basic EU regulation of 29.09.2003 but was attached to the EU Comments** of November 2003, which state that this document will nonetheless serve as a starting point.
IAS 1	Presentation of Financial Statements	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 2	Inventories	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 7	Cash Flow Statements	endorsed by the EU on 29.09.2003
IAS 8	Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 10	Events after the Balance Sheet Date	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 11	Construction Contracts	endorsed by the EU on 29.09.2003
IAS 12	Income Taxes	endorsed by the EU on 29.09.2003
IAS 14	Segment Reporting	endorsed by the EU on 29.09.2003
(IAS 15)	Information Reflecting the Effects of Changing Prices	**withdrawn by the IASB** following the other amendments; had already been endorsed by the EU and the **withdrawal will be decided on 1 October 2004 by ARC**
IAS 16	Property, Plant and Equipment	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 17	Leases	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 18	Revenue	endorsed by the EU on 29.09.2003
IAS 19	Employee Benefits	endorsed by the EU on 29.09.2003
IAS 20	Accounting for Government Grants and Disclosure of Government Assistance	endorsed by the EU on 29.09.2003
IAS 21	The Effects of Changes in Foreign Exchange Rates	endorsed, **amendments to be approved on 1 October 2004 by ARC**

[13] Source: ECB/Eurostat Accounting and Statistics Task Force (September 2004 meeting)

IAS 23	Borrowing Costs	endorsed by the EU on 29.09.2003
IAS-24	Related Party Disclosures	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 26	Accounting and Reporting by Retirement Benefit Plans	endorsed by the EU on 29.09.2003
IAS-27	Consolidated Financial Statements	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS-28	Investments in Associates	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 29	Financial Reporting in Hyperinflationary Economies	endorsed by the EU on 29.09.2003
IAS 30	Disclosures in the Financial Statements of Banks and Similar Financial Institutions	endorsed by the EU on 29.09.2003
IAS 31	Financial Reporting of Interests in Joint Ventures	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 32	Financial Instruments : Disclosure and Presentation	**to be approved on 1 October by ARC**
IAS 33	Earnings per Share	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 34	Interim Financial reporting	endorsed by the EU on 29.09.2003
IAS 36	Impairment of Assets	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 37	Provisions, Contingent Liabilities and Contingent Assets	endorsed by the EU on 29.09.2003
IAS 38	Intangible Assets	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 39	Financial Instruments : Recognition and Measurement	**to be approved on 1 October by ARC with "carve out" of the Fair Value Option and certain provisions for Hedge Accounting**
IAS 40	Investment Property	endorsed, **amendments to be approved on 1 October 2004 by ARC**
IAS 41	Agriculture	endorsed by the EU on 29.09.2003
IFRS 1	First-time Adoption of International Financial Reporting Standards	endorsed by the EU on 06.04.2004
IFRS 2	Share-based Payment	**new standard to be approved on 1 October 2004 by ARC**
IFRS 3	Business Combinations (**replaces IAS 22 " Business**	**new standard to be approved on 1 October 2004 by ARC**

	Combinations")	
IFRS 4	Insurance Contracts	**new standard to be approved on 1 October 2004 by ARC**
IFRS 5	Non-current Assets Held for Sale and Discontinued Operations (**replaces IAS 35 " Discontinuing Operations")**	**new standard to be approved on 1 October 2004 by ARC**

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