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Eurostat Activities on International Accounting Standards
Special Focus on Balance of Payments

Prepared by Eurostat

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1. Introduction

The European Commission is placing great emphasis on accounting harmonisation. The Internal Market Directorate General's aim is to improve the quality, comparability and transparency of financial information provided by companies.

According to the EU Regulation[1] on the application of International Accounting Standards (IAS), publicly traded companies will be required to apply from 2005 a single set of internationally agreed standards for the preparation of their consolidated financial statements. This will contribute to harmonise financial reports thus enhancing comparability across the European Union. Harmonisation of accounting rules will go to the benefit also of statisticians who are collecting data from enterprises in EU countries.

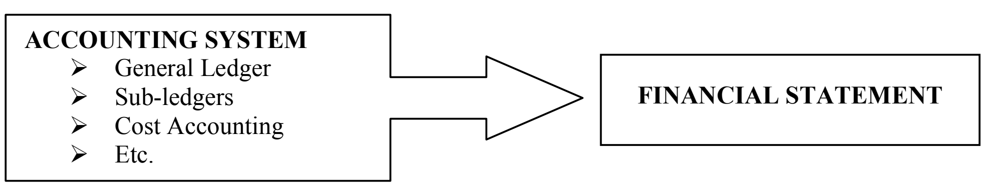
Member States will have the option to extend this requirement to unlisted companies and to the production of individual accounts: as a result, the degree of application of the IAS may differ from country to country.

The European Commission is working in parallel on the revision of the 4th and 7th Directives to ensure the compatibility between the Accounting Directives, which will remain applicable to all limited liabilities companies, and the International Accounting Standards.

2. Application of IAS: harmonisation of "output"

In the statistical field, harmonisation of "output" has already been achieved for major macroeconomic domains, both at the European level (by means of European Regulations, e.g. ESA 95), and at the international level (e.g. 1993 System of National Accounts, IMF Balance of Payments and Monetary and Financial Statistics manuals), where an agreed set of definitions and indicators has been defined. The result of this work is that statistical statements can be compared across countries, across institutional sectors and over time. The collection of data from respondents however remains a prerogative of each Member State and in practice collection systems differ.[2]

Hypothetically, the same input/output approach may be applied to accountancy, where the Financial Statements may be considered as one of the main output of the accounting system.



In each country the organisation of companies' accounting system is the result of historical and cultural differences. Nevertheless a shared European accounting system theoretically is attainable: countries and companies practices are evolving and are somehow connected with the harmonisation of commercial law (in this prospect it is worth mentioning the recent creation of the

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[1] Regulation (EC) no 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards.

[2] For example, in the BOP domain both surveys to companies and "indirect" reporting of international settlements by banks are used.

Societas Europaea[3]), companies tax regulation and with the world wide phenomenon of globalisation.

The introduction of **Harmonised Standards** does provide a common reference that defines evaluation principles and the content of the Financial Statements for disclosure.

According to IAS 1[4] (Presentation of Financial Statements), the Financial Statement is composed of:

1. Balance sheet
2. Income statement
3. Changes in Equity
4. Cash flow statement
5. Notes to the financial Statement

The main purpose of the IAS is to ensure comparability of the disclosed accounts, by setting guidelines for their structure and minimum requirements for the content.

These "official" statements are meant for a general purpose, which is to provide a wide range of users with information about the financial position, performance and cash flows of an enterprise. For Financial Institutions additional requirements are set out in IAS 30.

Ideally if the statistical information is already disclosed in the Financial Statements and if accounting and statistical concepts are harmonised, no additional burden is set on companies. In many countries the information can be readily available to statisticians via databases of companies' Financial Statements.

The accounting system in its broad sense is much more detailed than the information disclosed. In particular the general Ledger includes all accounts of a company. It varies depending on the size and complexity of a company's transactions. At the end of each accounting period, all transactions and positions recorded in the Ledger are the object of certain adjustments in order to comply with the accrual system and proper financial recording. Unfortunately at end of period other special recording are sometimes carried out to "make up" the result of the company performance so as to disclose a desired picture (the so called "window dressing").

The Financial Statement is not the only "output" of the accounting system, which also provides other types of information and reports for different purposes, both for the internal management and for external authorities (such as tax, administrative and statistical bodies).

3. Companies' accounts: a challenge for Balance of Payments compilers

The interest of BOP statisticians in accounting is increasing as data collection procedures are developing towards systems where companies become an increasingly important source of statistical information.

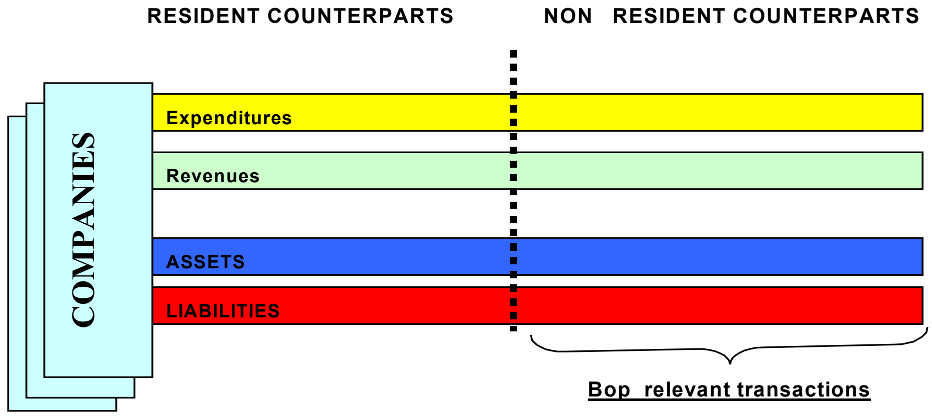
The shift in some EU countries of data sources for the collection of BOP data from bank settlements to companies' data is the result of a series of factors, such as the increasing complexity and diversity of international transactions, the development of Internal Market and the introduction of the Euro and the widespread use of practices like "cash pooling".

[3] A company may be set up within the territory of the Community in the form of a European public limited-liability company (Societas Europaea or SE) on the conditions and in the manner laid down in Council Regulation (EC) No 2157/2001 .

[4] The complete list of IAS document is given in Annex 1. Some of this document is currently undergoing a revision process.

Balance of Payments and accountancy concepts and output present a number of similarities. In particular the Financial Accounting records **all external transactions** (meaning transactions with third parties, residents or non residents) of a company.

This is quite similar to the information needs of Balance of Payments, but in this case transactions and positions with residents of the countries are not relevant. The Figure below highlights the sub-set of accounting data that are relevant for Balance of Payments purposes.



Also at the output level, Balance of Payments statements and Financial Statements present common concepts. The Current Account could be considered as an Income Statement (however there are some differences in classification for various transactions, such as fixed capital investments, changes in inventories, etc.), the International Investment Position (IIP) as a Balance Sheet and the Financial Account as the changes in Assets and Liabilities from one period to the other.

Several aspects however need to be considered.

From one side, the level of **detail of the information that will be disclosed** is of particular importance. Official companies' returns *per se* do not appear to be of great usefulness for BOP purposes. In fact the geographical aspect and the level of detail, in particular for the Services items, seem to be the most problematic areas. The IAS 14 on Segment Accounting deals in part with the issue of geography, but the minimum requirements for data disclosure in the Balance Sheets and Income Statements (IAS 1) do not include the split "resident/non resident" that would be of great interest to BOP statisticians. The information that is needed to compile the BOP and IIP in compliance with the National and International requirements will have to be found in the companies' ledger and sub ledger, and more generally, in the data stored in their data warehouse/ERP systems (e.g. records of orders, invoices, etc.). In this prospect, a major challenge is represented by the development of IT solutions for the accountancy and of ERP systems.

In any case, it is necessary to map the system to identify the moment the information is or could be collected, keeping in mind that each company is different and identifies the organisation of its accounting system so as to better monitor its performance.

The following questions should be addressed:

- Has the statistical data been recorded by the company and inserted in the (accounting) system?
- Are concepts in line regarding classification and evaluation?
- Is it feasible to retrieve the data at a reasonable cost?

- How can this information be made available to statisticians?

The objective is to limit the reporting burden and to obtain from companies data that are in line with the statistical requirements in terms of concepts and level of detail.

<u>Drafting survey forms and clear guidelines in accordance with accounting language makes reporting easier for companies. Furthermore clearly stating statistical needs and working towards harmonisation of concepts are to be considered as a means to save costs for the economic system in general.</u>

It is true that statistical needs are often considered as a burden to companies and requiring some information that was not originally classified may request efforts and manual intervention. Moreover one could expect that in case accounting and statistical concepts differ, companies' might follow the former also when compiling statistical returns.

Regarding **the comparison between accounting and statistical definitions and classifications,** some interesting areas that are being analysed are the evaluation principles of Financial Instruments (and the concept of fair value indicated by the IAS), and the treatment of specific transactions such as insurance, leasing, constructions. Of particular relevance is also the study of the accounting principles related to consolidation and disclosure of participation in Associates, as these concepts are linked to Foreign Direct Investment (FDI) and Foreign Affiliates Trade Statistics (FATS). An example of divergence between statistical concepts and the IAS is the definition of Associates. For FDI statistics, the concept of lasting interest is associated to a threshold of 10% while IAS 28 indicate that a "Significant influence" is presumed to exist if the investor owns more than 20 per cent of the Associate.

Both Eurostat and national BOP compilers have started an in-depth investigation on the links between Accountancy and Statistics. At Eurostat, the Technical Group Direct reporting is investigating best practices in obtaining data directly from companies. The TG has also organised a workshop on Accountancy and BOP. Its activity is co-ordinated with the work carried out by the Accounting Task Force set up in Eurostat, Directorate D (see next paragraph).

Furthermore, at the request of the European Round Table of Industrialists (ERT) a "European Steering Group for Multinationals" has been created to promote the testing of harmonised BOP reporting format for multinational enterprises. The exercise aims at assessing the feasibility of common forms with a close link with the accounting systems, in order to foster efficiency and quality of reporting across Europe. Special attention is also given to IT aspects, which are considered to have a significant impact on statistical work and contacts have been taken with major software companies. The results of the first contacts with major European multinationals indicate that **common understanding of information needs and data availability goes to the benefit of both statisticians and enterprises, by offering a better correspondence between statistical requirements and companies' accounting**.

4. Accountancy: Opportunities and constraints for statisticians

In the field of Accounting and Statistics, Eurostat (Directorate D) has set up an Accounting Task Force with participation of several countries as well as representatives from DG Internal Market. The major statistical fields likely to be influenced by the introduction of IAS (National Accounts, Financial Accounts, Business Statistics, Business Registers, Balance of Payments, etc.) are also actively involved. This group will also integrate a representative from balance sheet data offices and other stakeholders in this domain: furthermore, it is planned to invite participation also from the EFRAG (European Financial Reporting Advisory Group).

High level meetings have already started involving EFRAG, CMFB representatives, ECB and Eurostat

Regarding possible influence of statisticians in the development of the standards, it is important to mention that the IAS Board is actively reviewing a number of the current standards and a number of changes and improvements are expected to result from this review. Under a separate project also IAS 32 (Financial Instruments: Disclosure and Presentation) and 39 (Financial Instruments: Recognition and Measurement) are under review. EFRAG recognises that IAS 39 currently gives rise to the greatest difficulties – particularly in the area of derivatives, repurchase agreements and hedge accounting. The calendar for such reviews is given in Annex 1.

5. Conclusions

Statisticians should follow the development of accounting principles as survey variables could be at risk of some change and, conversely, opportunities can be explored to obtain directly from the accountancy data, which would be closer to statistical needs. The opportunity to react and to participate in the revision process of the International Accounting Standards should be considered with special attention.

A main concern is related to the difference between accounting and statistical language. Accounting and statistical concepts are complex and comparing the two requires high competence.

It is important, however, to emphasise that basic principles like time recording, accruals, double entry accounting and stock and flows concepts are common to companies accounts, National Accounts and Balance of Payments.

Having a closer look at the source of statistical data, in the specific case of company accounts, is a crucial point. The challenge is mainly directed at finding synergies and opportunities in terms of costs for statistical reporting and in terms of convergence of concepts.

Statisticians should not miss the chance to actively interrelate with the relevant accountancy bodies and clearly state their needs, by all possible means, at European and national level[5]. The result is a higher quality of statistics and less reporting burden for companies.

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[5] The CMFB document 02/07/D.5 “International Accounting Standards” proposes future actions and divisions of responsibilities between EU and National statistical institutions.

Annex 1

INTERNATIONAL ACCOUNTING STANDARDS in existence at 1 March 2002

In bold are those 13 standards for which an exposure draft has been issued and comments are invited by September 2002 to International Accounting Standards Board.

Moreover an Exposure Draft of Proposed amendments to IAS 32 and IAS 39 is available in the IASB web site and comments to be received by 14 October 2002.

IAS No.*	Title
IAS 1	**Presentation of Financial Statements**
IAS 2	**Inventories**
IAS 7	Cash Flow Statements
IAS 8	**Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies**
IAS 10	**Events After the Balance Sheet Date**
IAS 11	Construction Contracts
IAS 12	Income Taxes
IAS 14	Segment Reporting
IAS 15	**Information Reflecting the Effects of Changing Prices**
IAS 16	**Property, Plant and Equipment**
IAS 17	**Leases**
IAS 18	Revenue
IAS 19	Employee Benefits
IAS 20	Accounting for Government Grants and Disclosure of Government Assistance
IAS 21	**The Effects of Changes in Foreign Exchange Rates**
IAS 22	Business Combinations
IAS 23	Borrowing Costs
IAS 24	**Related Party Disclosures**
IAS 26	Accounting and Reporting by Retirement Benefit Plans
IAS 27	**Consolidated Financial Statements and Accounting for Investments in Subsidiaries**
IAS 28	**Accounting for Investments in Associates**
IAS 29	Financial Reporting in Hyperinflationary Economies
IAS 30	Disclosures in the Financial Statements of Banks and Similar Financial Institutions
IAS 31	Financial Reporting of Interests in Joint Ventures
IAS 32	*Financial Instruments: Disclosure and Presentation*
IAS 33	**Earnings per Share**
IAS 34	Interim Financial Reporting
IAS 35	Discontinuing Operations
IAS 36	Impairment of Assets
IAS 37	Provisions, Contingent Liabilities and Contingent Assets
IAS 38	Intangible Assets
IAS 39	*Financial Instruments: Recognition and Measurement*
IAS 40	**Investment Property**
IAS 41	Agriculture

* Discontinuity in the numbering of IAS is due to the fact that some of the first standards have been superseded by more recent ones.

Reference documents

- *International Accounting Standards: Official text*
- *International Accounting Standards : Exposure drafts*
- *European Accounting Guide, 4th edition . Miller*
- *Commission Paper : Examination of the conformity between IAS 1 to IAS 41 and the European Accounting Directives, European Commission, April 2001*
- *CMFB document 02/07/D.5 "International Accounting Standards" prepared by Eurostat, directorate D.*