A TRUE AND FAIR VIEW OF IMPLEMENTATION OF THE IAS REGULATION IN THE EUROPEAN UNION

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Abstract: The Regulation of the European Parliament and the Council of the European Union on the application of international accounting standards, was a key instrument to enhance comparability and transparency of financial statements prepared by publicy traded companies, in order to ensure the completion of a single financial services market. Never the less, Member States were allowed to extend the application of IAS to unlisted companies and to individual accounts.

Key words: European Directives, IAS Regulation, IAS endorsement process

European Union accounting requirements contains primarily four Accounting Directives: the Fourth and Seventh Directives on the annual and consolidated accounts of companies, the Directive on the annual and consolidated accounts of banks and other financial institutions, the Directive on the annual and consolidated accounts of insurance undertakings. With the accelerating pressure towards the convergence of accounting standards, the existing directives do not meet the needs to facilitate the access of European global players that wish to raise capital on international securities markets.

In this context, the Accounting Directives proved to be (Linder, 2006):

- - difficult to integrate into national law and even more complicate to make work in practice;
- - sensitive to some political compromises as is the tendency to avoid reopening issues;
- - reflecting the accounting thinking at the time they were writen.

With the European Legislation silent on many aspects of accounting, in 1998, according to IASC statistics, some 210 European Union companies reported in accordance with IAS while 235 reported under US GAAP while, in 1999, 275 European Union companies used IAS. Both financial reporting frameworks were investor-oriented financial reporting systems that provide a high levels of investor protection

Globalization of capital markets, the consolidation of stock exchanges and the International Organization of Securities Commissions (IOSCO) work on harmonised requirements for stock exchanges as the IASC focused more on the standard-setting have created a unique momentum to to accelerate completion of the internal market for financial services in order to increase market efficiency and reduce the cost of raising capital for European Union companies.

Consequently, the Lisbon European Council of 23 and 24 March 2000 underlined the key importance of a single financial market and set the deadline of 2005 for all publicly traded companies to prepare their consolidated financial statements in accordance with one single set of accounting standards, namely International Accounting Standards (IAS).

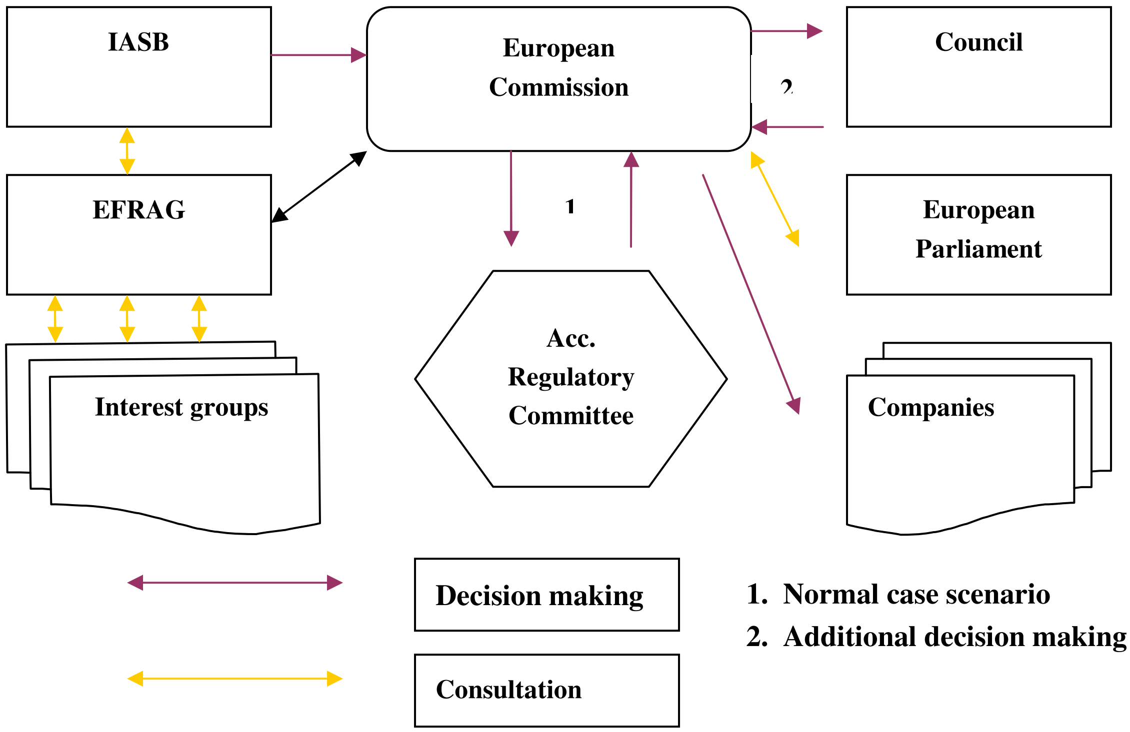
The Commission also, proposed that Member States to permit either to require or to allow unlisted companies as well as unlisted financial institutions and insurance companies**,** to publish financial statements in accordance with the same set of standards as those for listed companies.

Further more, the European Union Accounting Regulation gave European Union member states the option to:

- - Permit companies whose only listed securities are debt securities to delay IFRS adoption until 2007
- - Permit companies that are listed on exchanges outside of the EU and that currently prepare their primary financial statements using a non-EU GAAP (in most cases this would be US GAAP) to delay IFRS adoption until 2007.

In order to adopt an international accounting standard for application within the European Union, it is necessary to meet the basic requirements:

– they are not contrary to the "true and fair view" principle of the 4th and 7th Accounting Directives;
– they are conducive to the European public good (competitiveness and convergence);
– they meet the criteria of understandability, relevance, reliability and comparability.



IAS Endorsement process

Source: Linder, Financial Reporting Legislation in the EU, p.23

As the process for adoption of IFRS proceeded, proponents and opponents lined up for public hearing. The supporters believe that the European Union's strategy to adopt an international standard, rather than a particularly European one, has been validated (Zalm,2008). Overall, proponents highlighted that IFRS adoption is a project worth pursuing for three primary reasons:

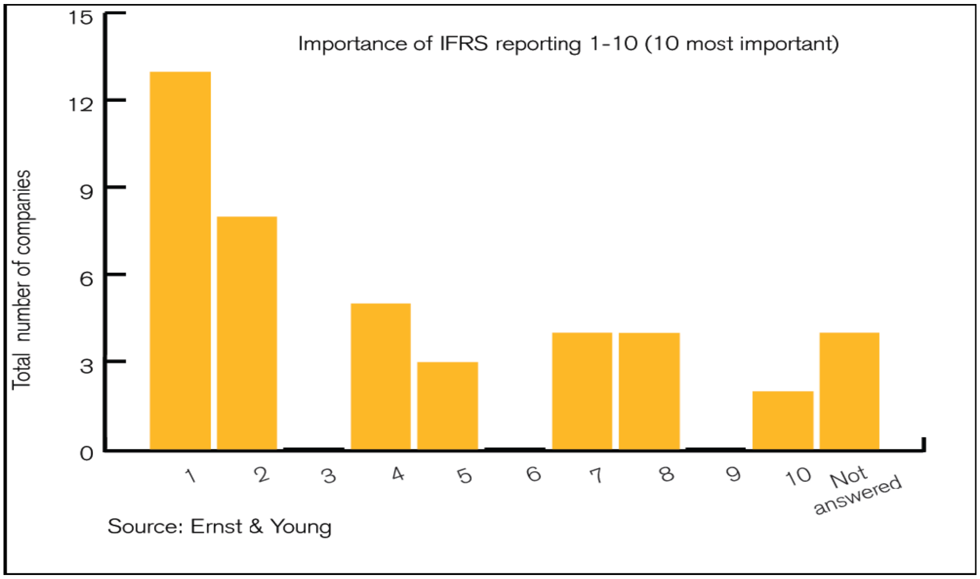
– IFRS can play a powerful role in providing transparency and comparability for investors rather than the application of domestic European standards;
– a single set of standards would lower the costs of of comparing performance of firms from different countries;
– European capital market would become more globally competitive as the result of massive capital flows from outside of Europe.

Nevertheless the European investors responded negatively to movement toward IFRS as the controversy focused on the suspicions that (Armostrong, 2007):

– the IFRS would not adequately reflect regional differences in economies;
– the IFRS would not accommodate differing political and economic member state features that led to existing differences across domestic accounting standards.
– the variation in the implementation and enforcement of IFRS would diminish any potential benefit

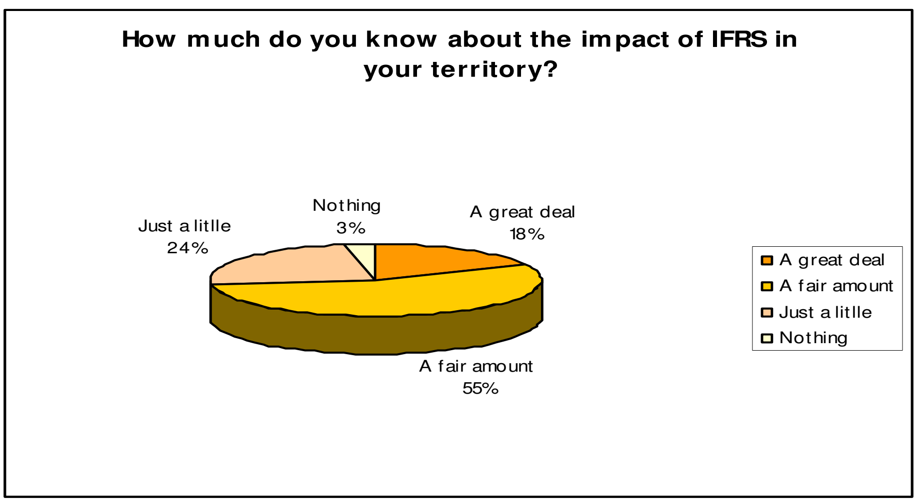
To assess the overall investor sentiment regarding IFRS adoption, we focused on the surveys on the effect of the transition to IFRS, conducted by major major polling organizations. Valuable lessons can be drawn from this researches.

Ernst & Young decided to carry out, in 2004, a pan- European survey of IFRS and the implications for the investment fund industry. The respondents were asked to rank the importance of IFRS reporting within their organisation on a scale from one (not important at all) to 10 (extremely important). The results were mixed, with 49% indicating low importance (ranks one to three) and 23% indicating high importance (ranks eight to 10).



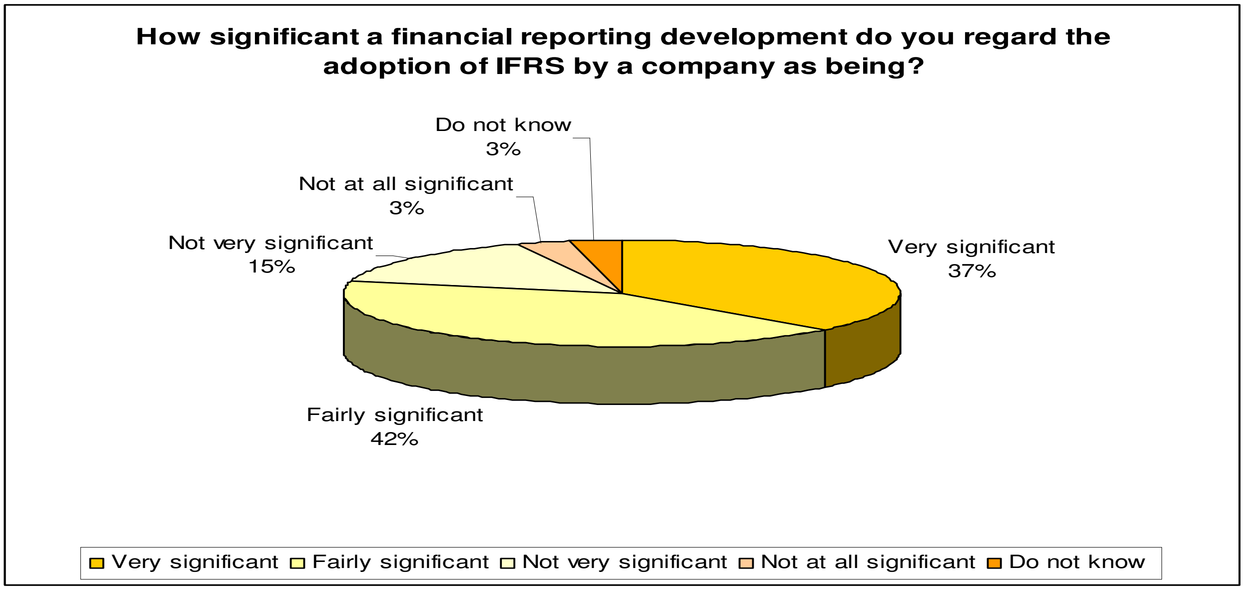
This survey demonstrated that there was a clear need for harmonisation and transparency with regard to the investment fund industry in Europe.

Another research was the PricewaterhouseCoopers /Ipsos MORI survey of 187 fund managers across Europe conducted in 2006. Most of the fund managers interviewed for the survey said they are fairly well-informed and understand the impact of IFRS. Nearly threequarters said they know either a lot or a fair amount about the impact of IFRS on companies in their country



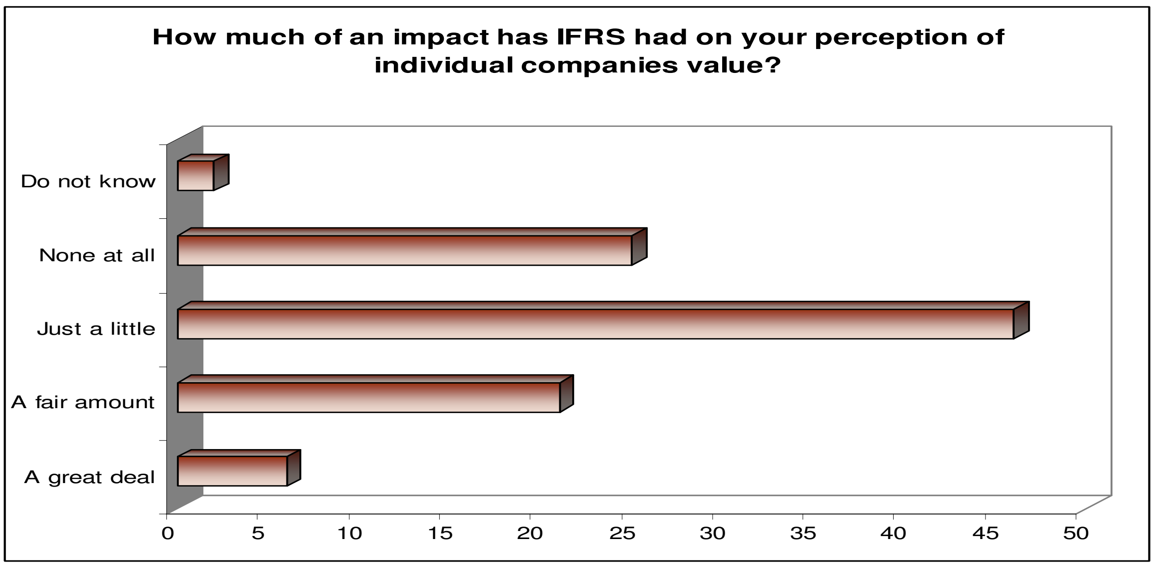
Source: PricewaterhouseCoopers /Ipsos MORI, 2006

Investment fund managers see the change to IFRS as significant. Four in every five believe that the adoption of IFRS is either a very or fairly significant development for financial reporting. The majority (66%) have already noticed its impact on the operational results of the companies they invest in.



Source: PricewaterhouseCoopers /Ipsos MORI, 2006

In spite of this encouraging results, IFRS had already affected fund managers' perceptions of value. Almost three-quarters said that the change to IFRS has had at least some impact on their view of the value of the individual companies they invest in, mainly because financial information is now easier to compare and offers greater transparency.

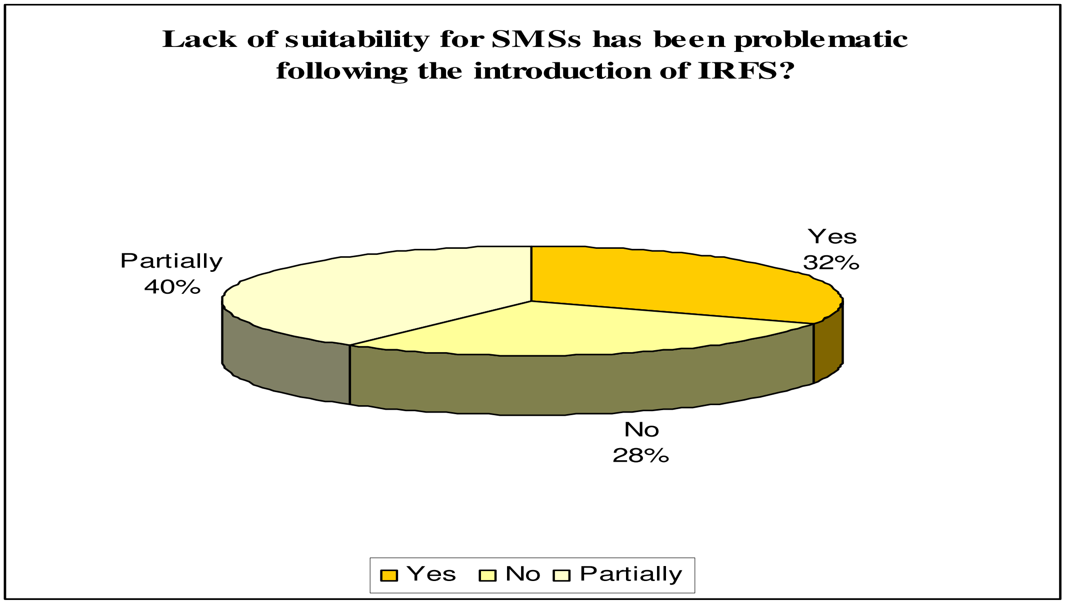


Source: PricewaterhouseCoopers /Ipsos MORI, 2006

Moves towards greater consistency of application, convergence, standardisation of requirements, and improved transparency, were high on the list of investors' hopes for the future development of IFRS, back in 2006.

The Association of Chartered Certified Accountants (ACCA) undertook a quantitative and qualitative survey of its members, in late 2007. This comprised in-depth focus groups with leading members in Poland, Hungary, the Czech and Slovak republics and Romania. The results were not encouraging for small and medium sized enterprises.

In the area of accounting regulation, ACCA focus groups members were largely supportive of the advent of International Financial Reporting Standards (IFRS) in Europe, believing it to have brought more meaning to accounts, which were previously taxdriven and of limited use for investors. Nevertheless the survey identifies the biggest problem which is the lack of suitability for SMEs.



Source: ACCA Central & Eastern Europe members' survey on SME issues, 2007

The results of this article reveal that the introduction of IFRS in Europe can be characterized as "a romantic project" which in time could prove to be a successful marriage or a painful divorce.

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