SOME DISCLOSURE ASPECTS REGARDING CONSOLIDATED FINANCIAL STATEMENTS

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Abstract: *The purpose of this article is to analyze the current state of consolidated reporting practice harmonization concerning the choice of presenting the income statement, the changes in equity, the methods used for presenting the cash flow statement, the extant methods for evaluating and reporting goodwill, the extant methods in which jointly controlled entities are accounted in the consolidated financial statements, or the choice for recognizing investments in subsidiaries, jointly controlled entities and associates in the separate statements of the parent company. In order to achieve our goal we selected the first 10 groups, in order of their capitalization value, that were listed on each of the following capital markets: London Stock Exchange, NYSE Euronext (Paris Stock Exchange) and Deutsche Börse (Frankfurt Stock Exchange) and we analyzed, in a qualitative and in a quantitative manner, for a period of six years starting with 2007, their consolidated financial statements with the design to establish exactly which of the aspects stated in the International Financial Reporting Standards were being used for the items presented above. In order to complete the empirical research part of the paper that addresses from a comparative perspective the evaluation of the degree of material harmony between the reporting practices of groups listed on the three stock exchanges above-mentioned, we used statistical and mathematical methods represented by the I Index first described by Van der Tas. Taking into account the fact that since 2005 all listed companies on the European stock exchanges were required to adopt the international accounting standards for their consolidated financial disclosures, the degree of material harmony was studied only in reference to those requirements that presented two methods or possibilities of disclosure.Our findings suggest that the groups analyzed present a high degree of material harmonization with respect to the reporting practices considered, especially in the last three years.*

Keywords: *consolidated financial statements; disclosure; IAS/IFRS; accounting harmonization.*

JEL classification: M41

1. Introduction

The preparation and presentation of consolidated financial statements has become, over time, a mandatory requirement for all group companies worldwide. This practice was first seen in USA and then was taken over by groups of companies in Europe. Nowadays, in Europe, listed groups should prepare a set of consolidated financial statements based on IFRS. This is required by EU Regulation no.1606/ 2002, which states that “member states are required to take appropriate measures to ensure compliance with international accounting standards” (EC, 2002). The obligation of listed groups to prepare consolidated financial statements based on IFRS, since

2005, comes as a first step, but also as a support for the efforts of regulators to implement a single set of international accounting standards accepted and used globally.
This paper brings into focus the analysis of some aspects which can give us a clearer picture of the presentation of information in the consolidated financial statements of listed companies in 3 stock exchanges with great impact on the European capital market, namely London Stock Exchange, NYSE Euronext and Deutsche Börse Group. The reason behind our choice of selecting the sampled data is described in the case study presented in third section of the paper.
First, we select the prior research findings, namely the literature review regarding the central theme of the article. Then, this research continues as follows: in the second section we present a brief description of the international accounting regulations concerning consolidated financial statements. In the third part, the empirical analysis of the disclosure of consolidated financial statements of listed groups is detailed in order to shape an idea about some important aspects for which IFRSs offer a choice. In the fourth part we expose our conclusions based on the findings in the case-study.

2. Literature Review

We consider that two streams of literature are relevant to our study: studies on the accounting harmonization process and studies investigating the consolidated financial statements and their disclosure according to the international or national regulations.
International accounting harmonization and convergence represent one of the most debated issues both in research literature and in practice. Harmonization scope allows making comparisons of international financial accounts easier, faster and cheaper (Carlson, 1997). Thus, in order to provide more transparent and comparative information, the accounting standards setters join their forces for issuing a single set of standards applicable to all entities around the world. The process of harmonization and convergence plays an important role for the accounting systems and was in the attention of researchers since early '80s. The prior studies having as central theme the measure of accounting harmonization can be grouped in two main categories: studies that measure the formal harmonization (de jure harmonization) and studies that measure material harmonization (de facto harmonization). The first category includes studies that quantify the degree of compatibility between the international accounting standards, IAS/IFRS and national accounting standards. In this case, the literature include, among others, the studies of Tay and Parker (1990), Rahman et al. (1996), Aisbitt (2002), Garrido et al. (2002), Fontes et al. (2005), Ding et al. (2007). The second category consists of research papers aimed at analyzing the degree to which the provisions contained in international accounting standards IAS/IFRS are actually implemented in the practice, or in the preparation of financial statements. In this category we can mention the following studies: Canibano and Mora (2000), Parker and Morris (2001), Rahman et al. (2002), Delvaille et al. (2005), Aisbitt (2006), Baltariu and Cirstea (2012).
Regarding the design and the presentation of consolidated financial statements, we found analyzed in the research literature four main theories, that have an impact on the disclosure of information in consolidated financial statements (Abad et al., 2000

Baluch et al., 2010: 1-12; Grossi and Gardini, 2012: 1-28; Müller, 2010: 56-63). All these research studies brought an added value to the topic of consolidated financial statements reporting.

3. International Referential for Consolidated Financial Statements

From the very beginning, the IASB has played an important role and had a substantial contribution to the international accounting harmonization process. The main objective of the regulatory body is to develop a single set of high quality, understandable, enforceable and globally accepted financial reporting standards based upon clearly articulated principles. There have been issued until now a number of 41 IASs and 13 IFRSs applicable to profit-oriented entities. Since 2001, almost 120 countries have required or permitted the use of IFRSs for their companies listed on the stock markets pioneering the way towards a global accounting harmonization. This trend of using a single set of accounting standards for reporting brings us to mind the following question "Can all accountants worldwide speak the same language?" (Rezaee et. al, 2010). Actually, the regulatory body committed to reduce the differences concerning the preparation and presentation of the financial statements, doing this because the financial reporting plays a key role in decision making. So, in other words, the financial statements are the main vehicle of information available for all users (Muniain, 2003). The financial statements are considered a key accountability tool for different users. Increasing relevance of financial statements is due to the existence of evidence of limited financial resources whose use must take into account social needs, the interest of stakeholders, the citizen rights, the quality and efficiency of the public services (Nistor and Stefanescu, 2012). The International standards underlying the preparation and presentation of consolidated financial statements are now: IFRS 10, 11 and 12. These were issued in 2011 and are applicable from 1 January 2013, actually replacing IAS 27, 28 and 31 which until 2013 were the basis for the preparation and presentation of consolidated financial statements of listed groups. Below we will briefly present the objective of each standard that was the basis of the preparation and presentation of consolidated financial statements of groups subject to our empirical study, namely IAS 27, 28 and 31.

Thus, IAS 27 has the twin objectives of setting standards to be applied: in the preparation and presentation of consolidated financial statements for a group of entities under the control of a parent; and in accounting for investments in subsidiaries, jointly controlled entities, and associates when an entity elects, or is required by local regulations, to present separate (non-consolidated) financial statements. IAS 27 Consolidated and Separate Financial Statements outlines when an entity must consolidate another entity, how to account for a change in ownership interest, how to prepare separate financial statements, and related disclosures. Consolidation is based on the concept of "control" and changes in ownership interests while control is maintained are accounted for as transactions between owners as owners in equity. (IAS 27.1)

IAS 28 Investments in Associates outlines the accounting for investments in associates. An associate is an entity over which an investor has significant influence, being the power to participate in the financial and operating policy decisions of the investee (but not control or joint control), and investments in associates are, with limited exceptions, required to be accounted for using the equity method. IAS 28

applies to all investments in which an investor has significant influence but not control or joint control except for investments held by a venture capital organization, mutual fund, unit trust, and similar entity that are designated under IAS 39 to be reported at fair value with fair value changes recognized in profit or loss (IAS 28.1).
IAS 31 Interests in Joint Ventures sets out the accounting for an entity's interests in various forms of joint ventures: jointly controlled operations, jointly controlled assets, and jointly controlled entities. The standard permits jointly controlled entities to be accounted for using either the equity method or by proportionate consolidation. IAS 31 applies to accounting for all interests in joint ventures and the reporting of joint venture assets, liabilities, income, and expenses in the financial statements of venture owners and investors, regardless of the structures or forms under which the joint venture activities take place, except for investments held by a venture capital organization, mutual fund, unit trust, and similar entity that (by election or requirement) are accounted for as under IAS 39 at fair value with fair value changes recognized in profit or loss (IAS 31.1).

4. Empirical Analysis – Case Study

4.1. Description of Study-Sample

As we can see in table 1, the groups included in our study were selected from the largest European capital markets, London Stock Exchange, Paris Stock Exchange and Frankfurt Stock Exchange, respectively. According to the European Federation of Stock Exchanges – FESE – taking into consideration the criteria of trade value and of turnover value, in January 2013, London Stock Exchange, NYSE Euronext and Deutsche Börse Group (Frankfurt Stock Exchange) were the largest stock exchanges in the European capital market (European Equity Market Report, 2013). From NYSE Euronext we selected Paris Stock Exchange as we considered it having the largest size and capitalization values. Afterwards, from each stock exchange we selected the first ten groups of companies included in the trading indexes FTSE100 (London Stock Exchange), NYSE Euronext100 (Paris Stock Exchange) and DAX30 (Frankfurt Stock Exchange) and considered them in order of their capitalization value. From the sample we excluded the groups which operate in the financial sector. Table 1 presents the remaining sample of groups included in our analysis. In order to extract the necessary information for our study, we consulted the documents containing the consolidated financial statements of the groups and the parent company individual financial statements (in most of the cases). The aria of documents studied was comprised of the Annual Reports, the Reference Documents and the Financial Reports which were published on the groups' websites. All the groups considered were obliged to comply with the international financial reporting standards regarding their consolidated disclosures. The period analyzed included six years, namely: 2007, 2008, 2009, 2010, 2011 and 2012.

Table 1: Study Sample

No.	Company Name		
	London Stock Exchange	*Paris Stock Exchange*	*Frankfurt Stock Exchange*
1.	Vodafone Group plc.	Sanofi	SAP AG
2.	BP Plc.	Total	Siemens AG
3.	GlaxoSmithKline Plc.	L'Oréal	Bayer AG
4.	British American Tobacco Plc.	LVMH Moët Hennessy-Louis Vuitton	Basf SE
5.	Royal Dutch Shell Plc.	GDF Suez	Daimler AG
6.	SABMiller Plc.	Danone	BMW Group
7.	Diageo Plc.	EADS N.V.	Deutsche Telekom AG
8.	Rio Tinto Plc.	Schneider Electric	E.ON SE
9.	BHP Billiton Plc.	Air Liquide	The Linde Group
10.	AstraZeneca Plc.	EDF Electricité De France	Volkswagen AG

Source: Authors Analysis

4.2. Research Methodology and Results

This article approaches the theme of material (de facto) accounting harmonization within consolidated financial disclosures from an international perspective. De facto accounting harmonization is studied with respect to several elements and methods which will be presented in short in the next paragraph. The elements which we selected for analysis refer to disclosure requirements which are mandatory but present two possible methods of application. The choice of the method to be used in order to fulfil the disclosure requirement belongs to the entities. These methods regard the presentation of consolidated financial statements; the practices with respect to evaluation and reporting of goodwill and of joint ventures, more specifically of jointly controlled entities, known also as joint arrangements from IFRS 12 Disclosure of Interests in Other Entities (issued by the IASB in May 2011); and the evaluation and reporting of investments in subsidiaries, joint ventures and associates in the parent company individual financial statements. As we mentioned above, our analysis comprises several elements which are synthesized as follows:

- Element number 1 (E1): the disclosure requirement regarding the presentation of results of operations, as stated in IAS 1 Presentation of Financial Statements, which currently allows groups the choice of disclosure of either *a single, continuous statement* (method 1), or two separate statements – *an income statement* and *a statement of comprehensive income* (method 2).
- Element number 2 (E2): in the case of presenting the results in two separate statements, the disclosure of other comprehensive income can be done either in *a statement of comprehensive income* (method 1), or *in a statement of recognized income and expense directly in equity* (method 2).
- Element number 3 (E3): the disclosure requirement regarding changes in equity, which is stated in IAS 1. In this case we observed that some groups preferred to disclose the information regarding the changes that had occurred in equity in a separate statement – *the statement of changes in*

equity (method 1) – while other groups chose to disclose this information only in the *Notes to Consolidated Financial Statements* (method 2).

- Element number 4 (E4): as stated in IAS 7 Statement of Cash Flows, this statement may be drafted by using either *the direct method* (method 1), which shows each major class of gross cash receipts and gross cash payments, or *the indirect method* (method 2), which adjusts accrual basis net profit or loss for the effects of non-cash transactions.
- Element number 5 (E5): regarding the practice concerning the evaluation and reporting of goodwill, IFRS 3 Business Combinations allows the choice between *the full goodwill approach* (method 1) and *the purchase goodwill approach* (method 2). In the case of full goodwill approach, the total amount of goodwill (the parent company share, as well as the minority interests incumbent value) is taken into consideration and evaluated and the initial recognition is done based on the price paid by the acquiring company for purchasing the net assets of the acquire. Under the purchase approach, goodwill is presented as being equal to the amount (price) paid by the acquiring entity, considered at fair value, minus the fair value of the net assets of the acquired.
- Element number 6 (E6): with respect to interests in jointly controlled entities, the groups have a choice between: *the proportionate consolidation method* (method 1), whereby the group's proportionate interest in the assets, liabilities, revenues and expenses of jointly controlled entities are recognized within each applicable line item of the financial statements; or *the equity accounting method* (method 2), which involves recording the investment initially at cost to the group, including any goodwill on acquisition and adjusting in subsequent periods the carrying amount of the investment as to reflect the group's share of the jointly controlled entity' post-acquisition profit or losses and its share of post-acquisition comprehensive income.
- Element number 7 (E7): refers to the parent company individual financial statements in which the investments in subsidiaries, jointly controlled entities and associates are allowed to be recognized either *at fair value* (method 1), as stated in IFRS 3, or *at cost* (method 2), as stated in IAS 27 Consolidated and Separate Financial Statements.

The research methodology of the present paper includes both qualitative and quantitative research methods. Among the qualitative research methods the analysis of documents, the analysis of consolidated financial statements of groups included in the study-sample, the comparative and the interpretative methods are distinguished. As to the quantitative research methods, in order to complete the empirical research part of the paper that addresses from a comparative perspective the evaluation of the degree of material harmony between the reporting practices of groups listed on three stock exchanges, namely London Stock Exchange, Paris Stock Exchange and Frankfurt Stock Exchange, we used statistical and mathematical methods represented by the *I Index* first described by Van der Tas, 1988: 165-168. The I Index is a measurement method of financial reporting practice harmonization at an international level, which focuses on "the degree to which the companies in one country apply the same or only a limited number of alternative accounting methods, compared to the companies in another country" (Van der Tas, 1988: 165). Taking into account the fact that since 2005 all listed companies on the European stock exchanges were required to adopt the international accounting