Chapter 3
Comparative Accounting: Europe

Discussion Questions

1. Regulating and enforcing financial reporting is a government function in France. The National Accounting Board (CNC) and the Accounting Regulation Committee (CRC) set accounting standards under the jurisdiction of the Ministry of Economy and Finance. The Financial Markets Authority (AMF) ensures compliance with French accounting rules (for listed companies). It is also a government agency.

   Public and private sector bodies are involved in the regulation and enforcement of financial reporting in Germany. The German Accounting Standards Board is a private sector body that develops German reporting standards for consolidated financial statements. However, German law (the HGB) governs financial statements at the individual company level. Enforcement also involves private and public sector bodies. The Financial Reporting Enforcement Panel is a private sector body that investigates compliance and relies on companies to voluntarily correct any problems that it finds. Matters that cannot be resolved are referred to the Federal Financial Supervisory Authority, a government agency, for final resolution.

   The regulation and enforcement of financial reporting is in the public sector in the Czech Republic. The Ministry of Finance is responsible for setting accounting principles and it also oversees the Czech Securities Commission which is responsible for enforcing compliance with Czech requirements. Some observers question the effectiveness of the Czech system.

   A private sector group is responsible for regulating financial reporting in the Netherlands. The Dutch Accounting Standards Board issues guidelines on acceptable accounting principles. Enforcement is handled by the Enterprise Chamber, a special accounting court. It rules on whether companies have used acceptable accounting practices, but only after an interested party has brought a complaint. The Financial Reporting Supervision Division of the Netherlands Authority for Financial Markets is responsible for enforcing reporting requirements for listed companies.

   Regulation of financial reporting is in the private sector in the United Kingdom. The Accounting Standards Board determines Financial Reporting Standards. The authority of the ASB is set out in the law. Two groups are responsible for enforcing financial reporting standards, one in the private sector and the other in the public sector. The Financial Reporting Review Panel (private sector) and the Department of Trade and Industry (public sector) can investigate complaints about departures from accounting standards. If necessary, they can go to court to force companies to revise their financial statements.

2. Given the requirement that all EU listed companies must use International Financial Reporting Standards in their consolidated financial statements, all five countries follow fair presentation principles for this group of companies' financial statements. The difference among the countries comes with listed companies' individual financial statements and with nonlisted companies. The overall picture is quite confusing.

   At the individual company level, France and Germany require local accounting standards.

Both can be characterized as legal compliance, conservative, and tax-driven. Individual company financial statements in the Netherlands and United Kingdom may use either local requirements or IFRS. However, in either case the result is fair presentation financial statements. The Czech Republic requires IFRS in listed companies' individual company financial statements, so the result is that they are fair presentation. In all five countries, nonlisted companies may use either IFRS or local accounting standards for their consolidated financial statements. As characterized above, the resulting financial statements will be quite different for German and French companies. Czech accounting standards are mostly fair presentation, but there is still some tax influence. Thus, the resulting financial statements can also be different depending on the choice that companies make. Finally, nonlisted companies' individual financial statements must be prepared under local accounting standards in the Czech Republic, France, and Germany. Local accounting standards or IFRS may be used by this group of companies in the Netherlands and United Kingdom.

3. The recently established auditor oversight bodies discussed in this chapter are:
   a. France—Haut Conseil du Commissariat aux Comptes (High Council of External Auditors)
   b. Netherlands—Netherlands Authority for Financial Markets
   c. United Kingdom—Professional Oversight Board

   The oversight body in France is in a government agency, whereas the one in the United Kingdom is a private sector body. The Dutch body is an autonomous administrative authority under the Ministry of Finance. They are a response to recent accounting scandals and represent efforts to the tighten control over auditors.

4. Consolidated financial statements are the statements of a group of companies under common management or control. Individual company financial statements are the statements of the separate legal entities (parent and subsidiaries) that make up the group. EU countries prohibit IFRS for individual company financial statements when these statements are the basis for taxation and dividend distributions. They are "legal compliance" countries (see Chapter 2) and individual company financial statements must comply with the law. Other countries permit or require IFRS for individual company financial statements because they are "fair presentation" countries (Chapter 2). Individual company financial statements are not the basis for taxation or dividends. Local accounting standards follow fair presentation principles.

5. This quote paraphrases a statement in the preamble to the charter establishing the German Accounting Standards Committee. We agree. Private sector initiatives (self-regulation) have been more successful than governmental initiatives in developing financial reporting regulations for national and international capital markets.

   Two noteworthy examples are the Accounting Standards Board in the United Kingdom (discussed in Chapter 3) and the Financial Accounting Standards Board in the United States (discussed in Chapter 4). Both have been flexible and adaptable in developing reporting standards in response to new circumstances. They are arguably the premier national standard setting bodies in the world. It is also noteworthy that Germany (Chapter 3) and Japan (Chapter 4) have recently moved to establish private sector organizations.

Chapter 8 discusses international harmonization and convergence. There, the work of the International Accounting Standards Board and the European Union are discussed. The EU was not effective in establishing standards for capital markets and has now endorsed the efforts of the IASB.

6. Existing French companies' legislation in the form of the Plan Comptable Général and Code de Commerce have the greatest influence on day-to-day French accounting practices. The two other authoritative sources of financial accounting standards and practices have comparatively modest or sporadic influence.

7. The statement is true. The German Accounting Standards Board is a private-sector body like the FASB (United States), ASB (United Kingdom), and IASB. The process for establishing standards is also similar. Working groups examine issues and make recommendations to the Board. These groups represent a broad constituency. GASB deliberations follow a due process and meetings are open.

8. Accounting requirements in the Czech Republic are based on EU Directives. Examples noted in the chapter are the following:
   a. True and fair view embodied in the Accountancy Act.
   b. Required audit.
   c. Statement of cash flows not a required financial statement (though it is required in the notes).
   d. Disclosures of employee information and revenues by segment.
   e. Consolidated financial statements required.
   f. Abbreviated reporting requirements for small companies.
   g. Notes include accounting policies.
   h. Listed companies use IFRS in consolidated financial statements.

   The accounting measurements discussed are also consistent with EU Directives, for example, the requirement for the equity method.

9. The Dutch Enterprise Chamber of the Court of Justice of Amsterdam helps ensure that filed or published Dutch financial statements conform to all applicable laws. Shareholders, employees, trade unions, or public prosecutors may bring proceedings to the Chamber by alleging that officially filed or published financial statements do not conform to applicable requirements.

   The Enterprise Chamber carries out its mission by determining whether the allegations of deficient financial reporting are true and how material such deficiencies are. Depending upon the case, the Chamber may require that financial statements be modified or it may seek penalties through the Court of Justice.

   The Chamber is composed of three judges and two Dutch RAs. There is no jury. Appeals of any of the Chambers rulings are difficult, may only be lodged with the Dutch Supreme Court, and are restricted to points of law.

10. British financial statements must present a "true and fair view" of a company's financial position and results of operations. The intent is similar to the U.S. "presents fairly" test. However, the "presents fairly" test in the United States is whether financial statements conform to U.S. GAAP. The "true and fair" test in the United Kingdom requires auditors to

step back and see whether the financial statements—taken as a whole—result in a fair presentation. U.K. GAAP may be overridden if complying with them would result in an “unfair” presentation. In other words, judgment is exercised in determining whether the financial statements are true and fair.

Exercises

1. *France*

   a. The Conseil National de la Comptabilité, or CNC (National Accounting Board) through the latest Plan Comptable Général and the Comité de la Réglementation Comptable, or CRC (Accounting Regulation Committee). The CNC and CRC are attached to the Ministry of Economy and Finance.
   b. The Autorité des Marches Financiers (AMF) for French listed firms. The Division of Corporate Finance (SOIF) conducts a general review of legal and other filings with the AMF. The Accounting Division (SACF) verifies compliance with accounting standards. The Ministry of Justice is indirectly responsible for compliance with reporting requirements by nonlisted companies through its role in supervising statutory auditors.

   Germany
   a. The German Accounting Standards Board for consolidated financial statements. Parliamentary legislation for individual company financial statements.
   b. The Financial Reporting Enforcement Panel (FREP). Matters that FREP cannot resolve are referred to Federal Financial Supervisory Authority (BaFin).

   Czech Republic

   a. The Ministry of Finance.

   b. The Ministry of Finance also has supervisory responsibilities. Audits are regulated by the Act on Auditors which established Chamber of Auditors to oversee the auditing profession.

   The Netherlands
   a. Dutch Accounting Standards Board.
   b. Dutch Enterprise Chamber of the Court of Justice in Amsterdam. Financial Reporting Supervision Division of the Netherlands Authority for Financial Markets for listed firms.

   United Kingdom

   a. Accounting Standards Board.

   b. Both the Department of Trade and Industry and the Financial Reporting Review Panel of the Financial Reporting Council can investigate complaints about departures from accounting standards and they can go to court if necessary to force compliance.

2. Good arguments can be made that France and Germany have the most effective accounting and financial reporting supervision mechanism for publicly traded companies. In France, the Autorité des Marches Financiers (AMF) is a government agency that supervises the stock market. It is the French equivalent of the U.S. Securities and Exchange Commission (SEC). Two divisions within the AMF enforce compliance with reporting rules. The Division of

Corporate Finance (SOIF) conducts a general review of legal and other filings with the AMF (including the annual report). The Accounting Division (SACF) verifies compliance with accounting standards. The AMF has the power to force compliance with accounting requirements. Germany has a two-tiered system. A private sector body, the Financial Reporting Enforcement Panel (FREP) reviews suspected irregular financial statements that come to its attention. It also conducts random review of financial statements. If companies do not voluntarily change their financial statements, FREP refers the matter to the Federal Financial Supervisory Authority (BaFin), a government agency that regulates the stock exchanges (and banking and insurance industries). In both countries, the agencies responsible for compliance are proactive. The responsibility in the Czech Republic is the Ministry of Finance, but there are many questions about its effectiveness. The responsibility in the Netherlands rests with the Enterprise Chamber. However, it isn't proactive—cases must be brought to it first. The Financial Reporting Supervision Division of the Netherlands Authority for Financial Markets is new (2006) but it can be expected to be effective. In the United Kingdom, the Financial Reporting Review Panel and the Department of Trade and Industry investigate complaints about financial reporting practices. It isn't clear how proactive either one is in enforcing reporting standards for publicly traded companies. The United Kingdom does not have the equivalent of the U.S. SEC. In our view, the most effective way to enforce accounting and financial reporting rules for publicly traded companies is through a government agency that is proactive in insuring compliance.

3. At the time of writing, the following accounting organizations discussed in this chapter were linked to IFAC's Web site:

   France

   Compagnie Nationale des Commissaires aux Comptes

   Conseil Supérieur de l'Ordre des Experts-Comptables

   Germany
   Institut der Wirtschaftsprüfer
   Wirtschaftsprüferkammer (WPK)

   Czech Republic

   Chamber of Auditors of the Czech Republic
   Union of Accountants of the Czech Republic

   The Netherlands

   Koninklijk Nederlands Instituut van Registeraccountants (Royal NIvRA)

   United Kingdom
   The Association of Chartered Certified Accountants
   Chartered Institute of Management Accountants
   Chartered Institute of Public Finance and Accountancy
   Institute of Chartered Accountants in England and Wales
   Institute of Chartered Accountants of Scotland

4. The question asked for five expressions, terms, or short phrases unfamiliar or unusual in the student's home country. Taking the United States as the home country, here are sixteen:

a. Duality in individual company and consolidated statements—the idea that the two sets of financial statements may be based on different GAAP, as in France in Germany.
b. Social report—required in France for companies with 300 or more employees, it describes, analyzes, and reports on matters of training, industrial relations, health and safety conditions, wage levels, benefits, and other work conditions.
c. Companies Act—national law regulating, among other things, financial reporting and disclosures by companies.
d. True and fair override—the idea in the United Kingdom that professional judgment can override a standard if necessary to give a true and fair view.
e. Provisions and reserves—used to smooth income and often based on tax laws, such as in Germany.
f. National chart of accounts—a formal chart of accounts designed for an entire economy and typically used for strong central economic control.
g. Secret reserves—undisclosed and deliberate understatements of assets or overstatements of liabilities.
h. Plan Comptable Général—French uniform national chart of accounts.
i. Sworn book examiners—a class of statutory auditors legally sanctioned in Germany to conduct independent audit examinations of companies.
j. Statutory auditors—Auditors who are required by law (statute) to audit a company's financial statements.
k. Enterprise Chamber of the Court of Justice of Amsterdam—a judicial institution receiving formal complaints of nonconformance with established Dutch accounting and reporting standards.
l. Generally acceptable accounting principles—accounting guidelines issued by the Dutch Accounting Standards Board in the Netherlands.
m. Proportional consolidation—consolidation technique often used for joint ventures where all assets and liabilities are prorated to the owners in strict proportion to their respective ownership interest percentages.
n. Legal reserves—appropriations of retained earnings required by law in most code law countries.
o. Coupon voucher privatization system—the method used by the Czech Republic to privatize large-scale, government-owned enterprises. Vouchers allowed CR citizens to buy shares for a nominal price.
p. Joint stock companies and limited liability companies—the terms used in the CR for corporations and limited liability partnerships, respectively. Joint stock companies issue shares whereas limited liability companies do not.

5. For each country discussed in the chapter, there are several financial accounting practices or principles at variance with international norms. The items below are illustrative only.
   a. France—Liabilities for post-employment benefits do not have to be recognized and finance leases do not have to be capitalized. Both accounting treatments are examples of form over substance and violate fair presentation. The treatment of post-employment benefits will understate reported earnings and understate reported liabilities. The debt-to-asset ratio will be understated. It is unlikely that an analyst will be able to adjust for this variance. The treatment of leases understates assets and liabilities, and understates the debt-to-asset ratio. The effect on income depends on how much lease payments differ from the amount of depreciation that would be recognized had the leased property been capitalized. It is unlikely that an analyst can adjust for this variance.
   b. Germany—Two different purchase methods are allowed, and goodwill can be treated several ways. The effects on reported earnings and the debt-to-asset ratio are unclear and it is unlikely that an analyst can adjust for these variances.

c. Czech Republic—Goodwill may be written off in the first year of consolidation or capitalized and amortized over a maximum of 20 years. The international norm is now to capitalize goodwill and impairments test it each year. If goodwill is written off immediately, there will be no effect on income compared to the international norm, except in a year where an impairments write-down would occur. The debt-to-asset ratio will be higher compared to the international norm. If goodwill is capitalized and amortized, reported earnings will be lower than what it would be under the international norm. As goodwill gets amortized, the debt-to-asset ratio will increase compared to the international norm. Analysts should be able to adjust to achieve "apples to apples" comparisons as long as the effects of the goodwill accounting are disclosed by Czech companies.
d. The Netherlands—Comprehensive current value accounting. Though only used by a minority of Dutch companies, this microeconomics approach to measurement is encouraged in the Netherlands to an extent not seen elsewhere. Expenses should be higher under current value accounting, especially for cost of goods sold and depreciation. This means that reported earnings will be lower. With higher asset values, the debt-to-asset ratio will decrease. Generally, the effects of applying current value accounting are disclosed in footnotes, so analysts should be able to adjust for this variance.
e. United Kingdom—Assets may be valued at historical cost, current cost, or a combination of the two. To the extent that current cost is used, the effects on reported earnings and the debt-to-asset ratio will be the same as described for Dutch current value accounting. Analysts will be able to adjust for this variance to the extent that the effects of using current costs are disclosed in the footnotes.

6. The country whose GAAP is most oriented toward equity investors appears to be the United Kingdom. Its GAAP is closest to IFRS, which is clearly aimed at equity investors. Under U.K. GAAP, goodwill may be capitalized and impairments tested, the IFRS treatment. LIFO is also not permitted, the IFRS treatment. The Netherlands comes in "second," but Dutch GAAP differs with IFRS on these two issues. The country whose GAAP is least oriented toward equity investors appears to be Germany, with France a close second. Germany has the most differences with IFRS.

7. The role of government in developing accounting and auditing standards is strongest in France. Government agencies are responsible for both activities and government involvement is all-encompassing. The private sector has little or no influence. The government plays the least role in the United Kingdom and the Netherlands. In both countries, the private sector is responsible for both accounting and auditing standards. Government influence is strong in Germany, but the German Accounting Standards Board is in the private sector and the German Institute is responsible for audit standards. The government is responsible for accounting standards in the Czech Republic (the Ministry of Finance), but auditing standards are developed by the Chamber of Auditors, a self-regulated professional body.

8. The European Commission has set up the European Group of Auditors' Oversight Bodies (EGAOB) to coordinate the new public oversight systems of statutory auditors and audit firms within the European Union. The EGAOB may also provide input to the Commission on issues such as endorsing International Standards on Auditing and assessing the public oversight systems in individual European countries. These public oversight systems have responsibility for overseeing:

a. The approval and registration of statutory auditors and audit firms
b. The adoption of standards on ethics, internal control of audit firms and auditing
c. Continuing education, quality assurance, and investigative and disciplinary systems.

At the time of writing, the EU Web site listed the following EU countries with an auditing oversight body:

a. Austria (Qualitätskontrollbehörde—Austrian Audit Quality Control Oversight Board)
b. Belgium (High Council for Economic Professions)
c. Bulgaria (Bulgarian Commission for Public Oversight of Registered Auditors)
d. Czech Republic—No auditing oversight body listed
e. Denmark (Danish Commerce and Companies Agency)
f. Estonia (Auditors' Professional Qualifications Committee)
g. Finland (The Auditing Board of the Central Chamber of Commerce of Finland)
h. France (Haut Conseil du Commissariat aux Comptes, H3C)
i. Germany (Abschlussprüferaufsichtskommission—Auditor Oversight Commission)
j. Greece (Accounting & Auditing Oversight Board)
k. Hungary (Auditors' Public Oversight Committee)
l. Ireland (Irish Auditing & Accounting Supervisory Authority)
m. Italy (CONSOB)
n. Latvia (Ministry of Finance)
o. Lithuania (The Authority of Auditing and Accounting)
p. Luxembourg (Commission de Surveillance du Secteur Financier)
q. Malta (Accountancy Board)
r. Netherlands (Netherlands Authority for the Financial Markets, AMF)
s. Portugal (Conselbo Nacional de Supervisao de Auditoria, Somissao do Mercado de Valores Mobiliarios)
t. Poland (Ministry of Finance)
u. Romania (Council for the Public Oversight of the Activity of the Statutory Audit)
v. Slovakia (Auditing Oversight Authority)
w. Slovenia (Agencija Republike Slovenije za javni nadzor nad revidiranjem, Agency for Public Oversight)
x. Spain (Instituto de Contabilidad y Auditoria de Cuentas, ICAC)
y. Sweden (Swedish Supervisory Board of Public Accountants)
z. United Kingdom (Financial Reporting Council—Public Oversight Board)

9.

	Accounting profession	Users/Preparers	Organized Labor	Tax Authorities	Commercial Law	Securities Commissions	Stock Market
France	Yes (some)	No	Yes (some)	Yes	Yes	Yes (some)	No
Germany	Yes (some)	No	Yes (some)	Yes	Yes	No	No
Czech Republic	Yes (some)	No	No	No	Yes	No	No
Netherlands	Yes	Yes	Yes	No	Yes	No	No
United Kingdom	Yes	Yes	No	No	Yes	No	Yes

10.

a. All countries require the purchase method, so there is no effect on the ratios for this method.

b. All countries require that goodwill be capitalized and amortized, so there is no effect on the ratios for this method. Compared to the IFRS treatment (capitalize and impairments test), the general effect is: (1) liquidity ratios unaffected; (2) debt-to-equity ratio unaffected; debt-to-asset ratio will be higher; (3) both profitability ratios will be lower.

c. The equity method is used in all five countries, so there is no effect on comparative ratios.

d. Current cost revaluations are allowed in the Netherlands and the United Kingdom. This practice results in higher asset values, higher equity, and lower income (because of higher depreciation and cost of goods sold charges). Both solvency ratios and both profitability ratios will decrease. The liquidity ratios should be unaffected.

e. German and French depreciation charges are tax-based, which are normally higher than economics-based depreciation. This will reduce income and lower the profitability ratios. The more rapid write-off of fixed assets will cause lower total asset values. Thus, the debt-to-asset ratio should increase. The debt-to-equity ratio and both liquidity ratios should be unaffected.

f. LIFO is permitted in Germany and the Netherlands, but not widely used. Companies using LIFO should have lower income, so lower profitability ratios. Inventory will probably be lower, causing the debt-to-asset ratio to increase and the current ratio to decrease. Cash flow to current liabilities will be unaffected.

g. Probable losses are accrued in all five countries, so there is no effect on comparative ratios.

h. Finance leases are not capitalized in France, Germany, and the Czech Republic. Companies will report comparatively lower noncurrent liabilities and noncurrent assets. Income will also be affected, but the amount is probably immaterial. The liquidity ratios should be unaffected. Both solvency ratios should be lower and return on assets will be higher. The effect on return on equity is probably immaterial.

i. Deferred taxes are not accrued in France and Germany, but they are not needed given book-tax conformity. The effects on the six ratios depend on other differences. The liquidity ratios are likely to be unaffected. The effects on the solvency and profitability ratios are unclear.

j. Income smoothing has an indeterminate effect on income in any given year. Therefore it is not possible to know how the profitability ratios are affected. The effect of creating reserves is to shift amounts that would otherwise be in retained earnings into the reserve accounts. Because both of these are in shareholders equity, this total is unaffected. Therefore, the solvency ratios are likely to be unaffected. The two liquidity ratios will be unaffected.

Case 3-1 Old Habits Die Hard

This case shows that old habits die hard and that requirements for information do not ensure that it will be provided.

1. The article suggests that the key feature of Czech financial reporting is a reluctance to disclose information. Sometimes information is disclosed, but only to those who ask for it. One may reasonably infer from the case that disclosures are probably not timely. One company offered to disclose information, but only if paid.

2. Apparently, Czech managers are only slowly recognizing the value of full and prompt disclosure to the investment community. There are several reasons for this. One is the 50-year legacy of Communism, where public disclosure was unnecessary or even inadvisable. Corruption is another lingering effect of Communism. Managers may fear the results of disclosure. Another is a lack of expertise in preparing required information; even if information eventually gets prepared, it may not be released on time. The case also notes that many companies were privatized because of government edicts, not because of management desires. Thus, managers are not motivated to provide information for the purpose of attracting outside capital. The aftermath of the privatizations in the 1990s (for example, tunneling) probably left many Czech citizens reluctant to invest in the stock market.

3. Investors kept in the dark will seek opportunities elsewhere. They will invest in other companies or in other countries besides the Czech Republic. Secretive companies lose when capital is not forthcoming. The stock exchange also loses. Stock exchange development depends on investor confidence which is supported, in part, by full and reliable disclosures of reliable financial information. Honest, open dealings are also necessary for investor confidence.

4. A program of changes needed to correct the problems identified in this case include the following:
    a. Improving accounting expertise through comprehensive professional education at universities in the Czech Republic. Resources need to be devoted to achieving this aim as well as business education in general.
    b. A system of laws emphasizing shareholder protection, and demanding full and complete disclosure of companies' financial position and results of operations. Current laws should be examined for weaknesses and omissions, and amended accordingly.
    c. Proper enforcement of shareholder protection and disclosure requirements. Government regulators should be appointed with the requisite accounting and legal expertise and with the necessary enforcement powers. They should have the authority to enforce compliance. Penalties are needed for noncompliance.

Case 3-2A What Difference Does It Really Make?

1. (Amounts in millions of euros)
   a.

	IFRS	U.S. GAAP	Percentage Difference
2006 net income	4,006	4,034	-0.7%
2006 stockholders' equity	45,600	46,023	-0.9%

   b.

	IFRS	U.S. GAAP	Percentage Difference
2005 net income	2,258	2,202	+2.5%
2205 stockholders' equity	46,128	46,403	-0.6%

   The percentage differences for net income and stockholders' equity are both close to zero for both years. However, as discussed next, the items responsible for most of the differences and the amounts of the items causing the differences vary between the two years. There are some large positive and large negative differences that just happen to net near zero. The key point about the comparisons is that they fluctuate between years. Therefore, reconciliations to U.S. GAAP require time specific information.

   c. The two largest reconciliation differences for 2006 are as follows:

   Income statement items: restructuring provision (+173) and Aventis business combination (+258 [783 - 525 = +258]).

   Balance sheet items: application of IFRS 1 (+6,356 [7,194 + 46 + (884) = +6,356]) and Aventis business combination (-5,879 [(1,115) + (4,031) + (733) = -5,879]).

   The two largest reconciliation differences for 2005 are as follows:

   Income statement items: application of IFRS 1 (-251 [(379) + (13) + 141 = -251]) and Aventis business combination (+217 [252 + (35) = +217]).

   Balance sheet items: application of IFRS 1 (+6,503 [7,426 + 52 + (975) = +6,503]) and Aventis business combination (-6,499 [(1,284) + (5,111) + (104) = - 6,499]).

   Because these differences arise from using IFRS, one would expect that other French multinationals are subject to similar item-by-item differences in their financial statements.

2. The financial statement reconciliations once required by the SEC for non-U.S. registrants would seem to be useful to U.S. readers of non-U.S. financial statements. Although the individual percentage changes are at best imprecise measurements, they convey a sense of the

direction of adjustments to be made as well as the relative sizes of any variations. This makes non-U.S. financial information at least roughly comparable with similar domestic U.S. information, and allows appropriate adjustments to financial ratios and other decision aids that rely on accounting information.

3. *Note to instructors*: This question will tweak students' interest in discussions of IFRS–U.S. GAAP differences and the SEC's decision to accept IFRS filings, as found in Chapters 4 and 8. The analysis above suggests a loss of information for investors. There are some significant individual differences between IFRS and U.S. GAAP as they affect net income and the balance sheet. The company discusses these differences quite extensively over several pages of its footnote disclosure. Of course, the question is whether IFRS and U.S. GAAP were sufficiently alike (converged) by 2007 to diminish the information value of the reconciliation. By now, most students should have heard of the IFRS–U.S. GAAP convergence project. Some of them may consult the Web sites of the International Accounting Standards Board and U.S. Financial Accounting Standards Board to see the status of the convergence project. If they do, they will likely conclude that many of the differences identified in this case are still to be resolved. Thus, one may wonder about the efficacy of the SEC's decision to exempt companies using IFRS from the reconciliation requirement. For further discussion of this issue, instructors can consult two commentaries in the June 2009 issue of *Accounting Horizons*, "Response to SEC Release, 'Acceptance of Foreign Private Issuers of Financial Statements Prepared in Accordance with International Financial Reporting Standards without Reconciliation to U.S. GAAP File No. 8713-07'" and "A Perspective on the SEC's Proposal to Accept Financial Statements Prepared in Accordance with International Financial Reporting Standards (IFRS) without Reconciliation to U.S. GAAP."

Case 3-2B Do The Differences Really Matter?

1. (Amounts in millions of euros)

a.

	IFRS	U.S. GAAP	Percentage Difference
2006 net income	5,015	4,385	+14%
2006 stockholders' equity	11,672	17,068	-32%

b.

	IFRS	U.S. GAAP	Percentage Difference
2005 net income	3,975	2,855	+39%
2005 stockholders' equity	8,765	15,396	-43%

The percentage differences for net income are not the same between the two years. IFRS income is 14 percent higher than U.S. GAAP net income in 2006 and 39 percent higher in 2005. The percentage differences for stockholders' equity are also not the same. IFRS stockholders' equity is 32 percent lower than U.S. GAAP stockholders' equity in 2006, and 43 percent lower in 2005. As discussed next, the items responsible for most of the differences and the amounts of the items causing the differences vary between the two years. The key point about the comparisons is that they fluctuate between years. Therefore, reconciliations to U.S. GAAP require time specific information.

c. The two largest reconciliation differences for 2006 are as follows:

   Income statement items: pensions and other similar obligations (-464) and profit/loss on disposal of group companies (-167).

   Balance sheet items: goodwill (+4,171) and indefinite-lived intangible assets (+1,246).

   The two largest reconciliation differences for 2005 are as follows:

   Income statement items: impairment of goodwill and intangible assets (-279) and pensions and other similar obligations (-265).

   Balance sheet items: goodwill (+4,531) and indefinite-lived intangible assets (+1,402).

   Because these differences arise from using IFRS, one would expect that other Dutch multinationals are subject to similar item-by-item differences in their financial statements.

2. The financial statement reconciliations once required by the SEC for non-U.S. registrants would seem to be useful to U.S. readers of non-U.S. financial statements. Although the individual percentage changes are at best imprecise measurements, they convey a sense of the direction of adjustments to be made as well as the relative sizes of any variations. This makes non-U.S. financial information at least roughly comparable with similar domestic U.S. information, and allows appropriate adjustments to financial ratios and other decision aids that rely on accounting information.

3. *Note to instructors*: This question will tweak students' interest in discussions of IFRS–U.S. GAAP differences and the SEC's decision to accept IFRS filings, as found in Chapters 4 and 8. The analysis above suggests a loss of information for investors. There are some significant individual differences between IFRS and U.S. GAAP as they affect net income and the balance sheet. The company discusses these differences quite extensively over several pages of its footnote disclosure. Of course, the question is whether IFRS and U.S. GAAP were sufficiently alike (converged) by 2007 to diminish the information value of the reconciliation. By now, most students should have heard of the IFRS–U.S. GAAP convergence project. Some of them may consult the Web sites of the International Accounting Standards Board and U.S. Financial Accounting Standards Board to see the status of the convergence project. If they do, they will likely conclude that many of the differences identified in this case are still to be resolved. Thus, one may wonder about the efficacy of the SEC's decision to exempt companies using IFRS from the reconciliation requirement. For further discussion of this issue, instructors can consult two commentaries in the June 2009 issue of *Accounting Horizons*, "Response to SEC Release, 'Acceptance of Foreign Private Issuers of Financial Statements Prepared in Accordance with International Financial Reporting Standards without Reconciliation to U.S. GAAP File No. 8713-07'" and "A Perspective on the SEC's Proposal to Accept Financial Statements Prepared in Accordance with International Financial Reporting Standards (IFRS) without Reconciliation to U.S. GAAP."