



Financial Statement Analysis  
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Yaso Thiru

**IAS/IFRS, US-GAAP and  
others: What is next?**

*The Demand on International Financial  
Reporting Standards*

# IAS/IFRS, US-GAAP and others: What is next?

## *Paper on International Financial Reporting Standards*

### **Introduction**

European Union regulation will be obligating the application of the IAS/IFRS for all capital market-oriented enterprises starting from the year 2005. For enterprises today already reporting on US-GAAP this will apply from beginning of 2007 (German Stock Exchange – Deutsche Börse allows application of IAS/IFRS and US-GAAP).

The International Financial Reporting Standards – IFRS, (formerly standards published as International Accounting Standards – IAS) are prepared and determined by the IASB (International Accounting Standards Board). It was founded as IASC (International Accounting Standards Committee) in the 70's by professional accounting associations of the industrialized countries. Meanwhile 41 standards and numerous additions are present.

By this regulation about 7000 quoted enterprises are directly concerned in the European Union. They will have to provide their consolidated accounting reports at the latest after 2005 according to the IAS/IFRS. At present only 275 quoted enterprises use the IAS/IFRS in the European Union. Since the early 90's German enterprises increasingly reporting on international accounting principles. The internationalization of the German economy and the demand of the capital markets for transparent and comparable enterprise numbers were responsible for this development.

## Main aspects

The traditional "Handelsgesetzbuch" (HGB) – German Commercial Law could fulfil these transparency requirements only insufficiently. Regardless of the partly open law situation multiplicity reasons demand the use of IAS/IFRS. From entrepreneur view the question about the raise of funds and venture capital is a basic element of the conversion from HGB to IAS/IFRS.

The new agreement on Basel II International Capital Framework created a serious change for the granting of loans. Internal or external Ratings should increase transparency to creditors on the applicants for the loan, in order to minimize the risks of receivables.

Besides the own equity ratio is an important issue for granting the loan. As a consequence there is the fear of higher interest and smaller chances to receive funds for entrepreneurs and in consequence personal loans.

The reporting on IAS/IFRS offers the chance to represent a more realistic picture of the future opportunities and financial situation of the enterprise. So for instance real estates according to the current market value can be located in the balance sheet.

In addition patents, brands or self produced assets can increase the value of assets in the balance. Some of the enterprises concerned will be able to improve their equity. That again offers advantages in the Rating methods in accordance with the Basel II-agreement, particularly the company's reputation on loan officers.

The reporting on IAS/IFRS (properly with a Restatement in US-GAAP) will increase the international comparability between enterprises of same or

different industries. Straight this comparability makes an adequate illustration for the economical substance possible for the enterprises concerned, particularly in the context of international investors. IAS/IFRS gives an enterprise on the international capital market a chance, to raise international funds and international loans up more intensive.

Apart from the advantages with financing issues, IAS/IFRS can also be useful for the acquisition of large assignments in international range. On many international bid invitations, financial statements must be delivered on international accounting principles.

### **Changes according to IAS/IFRS**

The HGB is depending on national tax law, while IAS/IFRS is independent and almost exclusively oriented at the information function for stakeholders.

The following table lists selected differences between HGB, IAS/IFRS and US-GAAP:

<b>Topic</b>	<b>HGB</b>	<b>IAS/IFRS</b>	<b>US-GAAP</b>
Superior Principle of Prudence „Vorsichtsprinzip“	X	Not superior	Not superior
Authoritative principle on national tax law	X	Independent	Independent
Disclosed Reserves „Stille Reserven“	X	Justified	Justified
GAAP - „GoB“	X	Framework	Conceptual Framework

*Table: Change according to HGB, IAS/IFRS and US-GAAP.*

### **An Example:**

The abolishment of the partial write off rules in the German Tax Law by the current cabinet, which remained still prescribed however in the German Commercial Law (HGB), so that the commercial balance sheet and the tax

balance contradict each other directly. This also happens based on IAS/IFRS Reporting Standards.

### The role of IFAC

The IFAC (International Federation of Accountants) is an umbrella organization of worldwide Certified Public Accountants (CPA). Their task is to develop concepts that improve financial management and financial statements. Furthermore they are in charge of compiling auditing standards to review annual reports, including the promotion of their acceptance.

Due to the complex relation between third parties and IFAC the following illustration is used to give a better understanding to the reader:

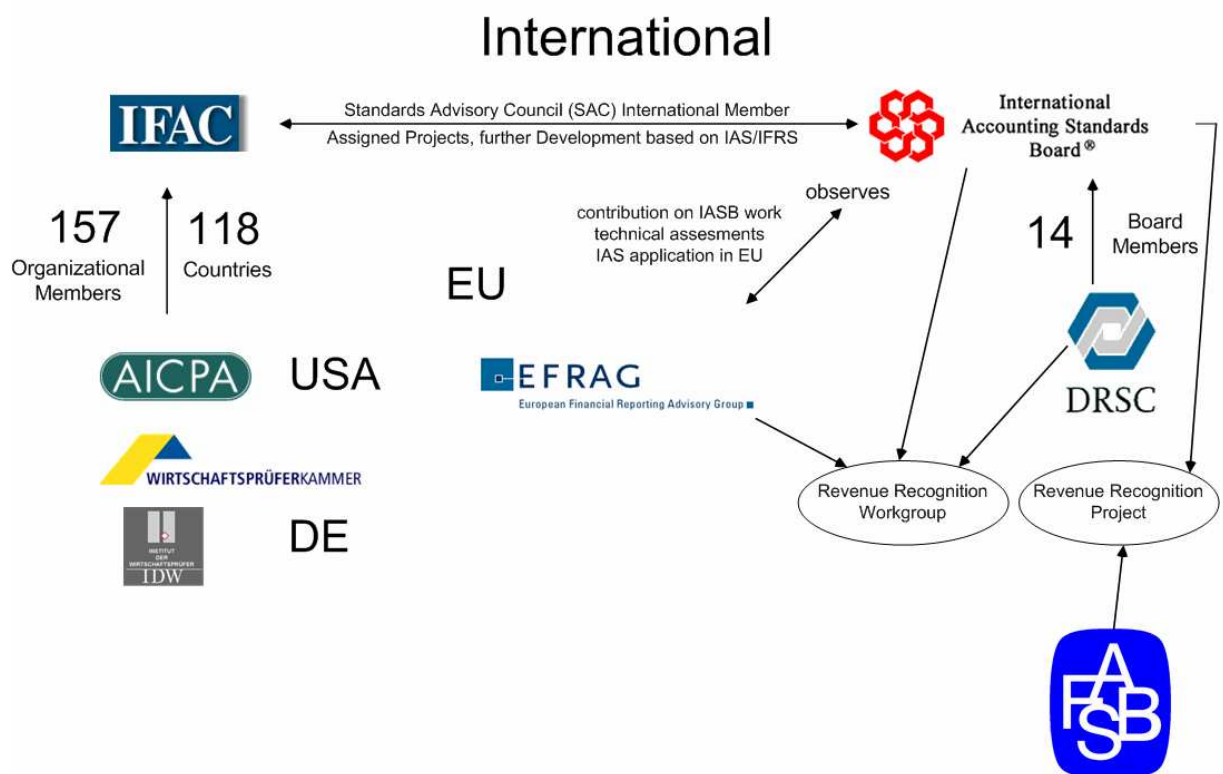


Illustration 1: Organizations and tasks related to IFAC

IFAC also received responsibility on projects assigned by IASB, due to resource reasons. IASB uses IFAC for its high specialist knowledge. IFAC also gives advice to IASB in Accounting Principle Development, in some cases IFAC is also in charge of further elaboration for accounting principles based on IAS/IFRS.

## Conclusion

The demand of global valid International Accounting Standards can be divided in two categories (compared to German Accounting Standards):

- ✚ Economy policy reasons (i.e. Globalization)
- ✚ Fair reasons
  - Undisclosed Reserves leading to deception of financial situation
  - Over weighted Superior principle of prudence
  - Authoritative principle (in relation to tax law)

The conversion of the balance statements of HGB to IAS/IFRS (01/01/2005) can lead to an increased transparency of the reporting enterprises, which can grant a better overview for all participating stakeholders. The major effects on the company's balance sheets (after 01/01/2005) will be:

- ✚ An Increase of assets
- ✚ An Increase of own equity

Explanation: Under special circumstances the activation for intangible assets and establishments in IAS/IFRS is allowed.

The harmonization of international accounting driven by an open discussion in targeted comprehensive committees to adopt them is essential for obtaining an accepted global accounting standard.

Furthermore local governments must understand the demand of unique reporting standards. That is a matter to adjust Tax Balance Sheets and Commercial Balance Sheet simultaneously by national regulations.

### **Readings**

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