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International Accounting Standards

from UK standards to IAS – an accelerated route to understanding the key principles

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Nothing is to be feared. It is only to be understood.

Marie Curie (1867–1934)

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Introduction

The World never stands still and the same is true of the business community and the people that comprise it. Business organizations strive to improve their profits, borrow to fund growth or sell assets to facilitate survival, but the one thing they can never do is stand still or at least not for very long.

Furthermore the commercial universe comprises not of a meagre handful of business entities but millions ranging in size from the sole trader to the international conglomerate. If all of these factors are combined there appears to be a recipe for chaos, but this is not the case. As the number and complexity of business organizations has increased so have the rules and guidelines that constrain them.

The balance between these two forces is always a matter for debate with some commentators stating that the entrepreneurial spirit of business is being crushed by red tape, whilst others look for increased controls following a series of high profile corporate frauds such as WorldCom which required a $74.4 billion restatement of income. These rules come from many sources:

- Corporate legislation
- Industry guidelines
- Listing requirements and other stock exchange rules for public companies
- Accounting standards.

Let us focus on the larger corporations as these will be represented by household names with which we can all associate. These usually have a large and diverse investor base plus interactions with many other stakeholder groups ranging from suppliers/customers to government. The most readily available source of information on the business for all these user groups is the published financial statements, and it should come as no surprise that these have evolved from a simple historic record of transactions as seen 50 years ago to the detailed multi-part document seen today. Since the 1990s the evolution of financial statements has had three main strands.

1. *Corporate governance* There is a general principle that the management team of a company will enter into transactions that are in the best interests of the shareholders and other stakeholder groups.

Sadly the confidence of these stakeholders has been undermined by a series of high profile frauds and it was one of these, namely the financial mismanagement at the Enron Corporation, which initiated a groundswell for improved corporate governance.

The concept of corporate governance asks 'how well the managers manage', and has seen a tidal wave of new legislation and best practice rules instigated in all the major investment markets around the World. Most noteworthy of these has been the Sarbannes–Oxley Act in the USA and the Combined Code in the UK.

Disclosures relating to corporate governance and the audit of its compliance are now an integral feature of published accounts.

2. *Social and environmental reporting* Unlike corporate governance the majority of the rules on reporting how a business interacts with the environment are voluntary, but with increasing awareness of issues such as global warming and sustainability of resources this looks set to change.

The absence of statute initially created the danger that only those organizations that were perceived as environmentally aware would provide stakeholders with details of their policies. However, this is rapidly changing as it becomes apparent that socially aware policies can improve brand perception and hence add to shareholder value.

3. *International harmonization* With the development of the Internet, increased ease of international travel and the development of companies through international growth and acquisition, the days when an investor would usually be based in the same country as the business in which they had invested have passed. This brings huge opportunities but also creates a dilemma for a potential investor trying to appraise the relative merits of expanding their portfolio into new markets.

The accounting rules and conventions of different countries have been developed when little regard was needed for international consistency. This insular approach has now been found wanting on the global stage, and so the wheels were set in motion towards the harmonization of these divergent rules.

Of all the changes identified above it is the latter that has proved the most daunting with a natural instinct for the creators of national accounting rules to advocate their own work, and the logistics of changing local legislation.

However, the drive to harmonize accounting is often perceived as a technical exercise that will occupy the brains of accounting academics but have little real bearing on the average stakeholder. Hopefully the fact that you have picked up this book means that you are aware this is not the case, but if you have any lingering doubts let us take a snapshot of the evidence.

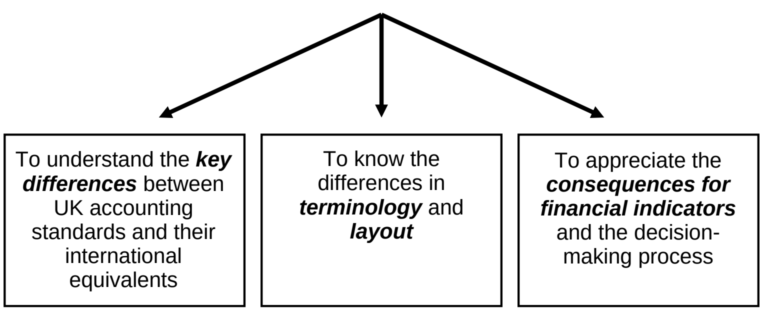
- Although harmonization is initially focussed on listed companies it has implications for businesses of every size either directly or indirectly through trading relationships.
- The reported performance and position of a business can be dramatically altered by the change to new accounting rules. Without an understanding of the main issues, investment appraisal could be seriously undermined.
- Providers of finance will need to review financial covenants included in funding agreements as the thresholds set may no longer be appropriate.

At this point you might be sensing a degree of trepidation envisaging the stacks of paperwork you need to read bulging with the technical jargon of accountants.

BUT

Fear not!

There is a sensible compromise between blissful ignorance and the finely tailored skills of a public company finance director – think what you really need.



The objective of this book is to provide a succinct and straightforward route map to meeting these needs. It will allow you to pick and choose subjects of particular interest or taken in aggregate provide a direct path to a big picture understanding of the consequences of the switch to international accounting – let us get to work!