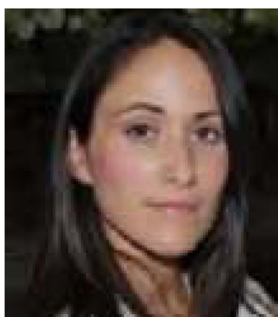
Transposition of the Accounting Directive

LIANA SAID

LIANA SAID IS AN ASSISTANT ADVISOR AT KPMG MALTA.



MONIQUE MICALLEF

MONIQUE MICALLEF LECTURES ON FINANCIAL ACCOUNTING AND REPORTING-RELATED TOPICS AT THE UNIVERSITY OF MALTA.

The Fourth and Seventh Accounting Directives failed to reach the desired comparability of financial statements in the EU, as member states had been provided with too many member state options (MSOs) to transpose in their national laws (Burggraaff, 1981). The adoption of these MSOs varies across the member states and this, together with the fact that all options under the Fourth and Seventh Accounting Directives had been used by at least one member state (EC, 2009), makes comparisons of financial statements in different member states difficult. Among other objectives, Directive 2013/34/EU (hereafter, 'Accounting Directive'), sought to address this issue but later stage political negotiations at European Council and European Parliament level resulted in 'new MSOs being introduced or existing MSOs being maintained' (EFAA, 2014, p.6) leading to over one hundred options (EFAA, 2014).

OBJECTIVES

Many of the MSOs found in the Fourth and Seventh Accounting Directives remained. The literature on international classification of accounting systems could predict that most of the MSOs available under the Accounting Directive could have been transposed in a manner similar to those provided under the superseded accounting directives. This article, which is based on a 2017 Master in Accountancy dissertation, investigates this with a focus on small entities. It also seeks to classify accounting systems, in accordance with selected MSOs, to provide insight into the extent of their similarity. The transposition details in the following nine member states were collected through the use of a questionnaire: Bulgaria, Czech Republic, Estonia, Germany, Ireland, Italy, Malta, Slovakia and Spain.

CLASSIFICATION OF ACCOUNTING SYSTEMS

'Classification can help to structure data and understand phenomena' (André, 2017, p. 2). There is a large body of literature focusing on international classifications of accounting systems. Papers with a specific coverage of Malta are looked at in this article. Malta first featured in the work conducted by Sellhorn and Gornik-Tomaszewski (2006), who propose a classification of accounting systems based on the choices available to member states in the IAS Regulation. Their study results in three groups. Looking at the implementation option related to for example, the individual financial statements of non-listed companies, Malta is classified as 'Level 1 - IFRS required for individual accounts - all types of firms', together with Cyprus. At that time, all companies in Malta were required to adhere with IFRS. The second group, 'Level 2 - IFRS permitted for individual accounts' includes countries were IFRS are permitted for all types of firms, such as Denmark, Finland, Germany, Greece, Hungary, Iceland, Ireland, Italy, Liechtenstein, Luxemburg, Netherlands, Norway, Portugal, and the UK. 'Level 3 - IFRS prohibited for individual accounts of all types of firms' includes Austria, Belgium, Czech Republic, France, Spain, and Sweden.

Malta then features in the related literature in the study conducted by Nobes (2008) who proposes a two-group accounting classification based on the strengths of the equity markets and the degree of cultural dominance. Malta features in 'Class A (strong equity, commercially driven)' together with seven other countries/ system: Cyprus, Denmark, Ireland, Netherlands, Norway, the United Kingdom and IFRS. The other twenty-one countries are included in 'Class B (weak equity, government driven, tax-dominated)'.

Malta is then included in the study conducted by Forst (2014) who proposes a hierarchy based on the implementation choices in the IAS Regulation. Forst's (2014) findings suggest that 'the macro-economic, political, and legal factors which gave rise to earlier classifications of accounting systems survive into the IFRS era…' (Forst, 2014, p.193). Hierarchical cluster analysis of the options provided in the IAS Regulation results in three clusters. Malta forms part of the 'IFRS integrated countries' cluster together with Bulgaria, Cyprus, Estonia, Greece, Italy, Latvia, Lithuania, and Slovakia. The 'IFRS leaning' group is comprised mainly of UK-influenced and Scandinavian countries: Czech Republic, Denmark, Finland, Iceland, Ireland, Leichtenstein, Luxembourg, Netherlands, Norway, Slovenia, and the United Kingdom. The 'IFRS antagonistic' group is comprised mostly of Continental European countries influenced by German and French accounting practice: Austria,

Belgium, France, Germany, Hungary, Poland, Portugal, Romania, Spain, and Sweden.

Following the transposition of the Accounting Directive across the member states, André (2017) classifies the accounting systems in twenty-five member states, based on the extent of convergence between IFRS and national GAAP of large, non-listed, non-financial entities. Five groupings are identified: (i) 'Full IFRS': Cyprus; (ii) 'Generally aligned with IFRS and referenced/acknowledged': Croatia, Denmark, Finland, Greece, Malta, Poland, Portugal and Slovenia; (iii) 'Generally aligned with IFRS for SMEs': Estonia, Ireland, Netherlands, Norway, Sweden, and the United Kingdom. The other countries are classified within the remaining two categories being (iv) 'Generally aligned with IFRS yet not referenced/ not acknowledged' and (v) 'Some alignment but single accounts have other focus'.

THE INFLUENCE OF PREVIOUS GAAP

A brief analysis of a number of selected MSOs common to both the Fourth Accounting Directive (FAD) and the Accounting Directive follows.

(i) The majority of the MSOs selected saw no resulting change in accounting treatment on the transposition of the Accounting Directive:

- Art 31(1)(a) of the FAD; art 6(5) of the Accounting Directive: Member states can permit or require the recognition of all foreseeable liabilities and potential losses arising in the course of the financial year or a previous financial year, even if such liabilities or losses become apparent only between balance sheet date and the date on which the balance sheet is drawn up.

- Art 4(2) of the FAD; art 9(3) of the Accounting Directive: Member states can permit entities to adapt the format of the balance sheet and profit and loss account.
- Art 2(5) of the FAD; art 4(4) of the Accounting Directive: Member states can define cases of departure from the provisions of the directive in exceptional cases and lay down the applicable relevant special rules.
- Art 42(e) of the FAD; art 8(1)(b) of the Accounting Directive: Member states can permit or require entities to value specific categories of assets other than financial instruments by referring to their fair value.
- Art 42(a)(5a) of the FAD; art (8)(6) of the Accounting Directive: Member states have the option to permit or require the recognition, measurement and disclosure of financial instruments in conformity with international accounting standards as adopted by the EU.
- Art 20(2) of the FAD; art 12(12) of the Accounting Directive: Member states can permit the creation of provisions intended to cover expenses which at the balance sheet date are either likely to be incurred, or certain to be incurred but uncertain as to amount or as to the date on which they will arise.

(ii) Other MSOs saw only one member state (the member state varies depending on the MSO) change its accounting treatment:

- Art 6 of the FAD; art 9(6) of the Accounting Directive: Member states can allow or require adaptation of the layout of the balance sheet and profit and loss account in order to include the appropriation of profit or the treatment of loss.
- Art 33(1)(c) of the FAD; art 7(1) of the Accounting Directive: Member states may permit or require entities to measure and present fixed assets at their revalued amounts.
- Art 59(1) of the FAD; art 9(7)(a) of the Accounting Directive: Member States can permit or require participating interests to be accounted for using the equity method.
- Art 59(1) of the FAD; art 9(7)(a) of the Accounting Directive: Member States can permit or require that the proportion of the profit or loss attributable to the participating interest be recognised only to the extent of the amount corresponding to dividends

already received or the payment of which can be claimed.

(iii) Minimal MSOs saw several member states change their accounting treatment:

- Art 11 and art 27 of the FAD; art 14(1) and 14(2) of the Accounting Directive: Member states can allow entities to draw up abridged balance sheets and/or abridged profit and loss accounts. Bulgaria, Czech Republic and Estonia previously disallowed the drawing up of an abridged balance sheet and/or profit and loss account, but are now permitting them under the Accounting Directive. Both Malta and Ireland previously allowed the drawing up of the abridged profit and loss account but this is now disallowed.
- Art 46(3) of the FAD; art 19(3) of the Accounting Directive: Member states can exempt small entities from preparing management reports in certain circumstances. Several member states have now taken up the option including Czech Republic, Estonia, Ireland and Malta.

Therefore, apart from the latter MSOs, overall small entities in different jurisdictions can still adhere to the same accounting treatment that they had adhered to prior to the transposition of the Accounting Directive. This suggests that the way options were transposed by member states under the FAD influenced the way the options were transposed under the Accounting Directive. Based on the options selected and on the participant member states, the Accounting Directive seems to have had a minimal effect on enhancing comparability between member states in relation to small entities.

CLASSIFICATION OF ACCOUNTING SYSTEMS

The Two-Step Clustering Classification procedure was utilised to classify the accounting systems relating to small entities in the nine member states. The clustering is carried out based on the similarities and differences in the options taken up or not, available in the Accounting Directive. Table 1 reveals the existence of two clusters with the two main determinant clustering variables relating to the MSOs on the abridged balance sheet and the abridged profit and loss account.

Most of the classifications reviewed earlier have a different focus such as the accounting systems related to large, listed entities or the IAS Regulation. Nobes (2008) classifies Ireland and Malta as Class A (strong equity and commercially driven) but Slovakia as Class B (weak equity, government driven, tax-dominated). Forst (2014) classifies Malta and Slovakia as IFRS integrated whilst Ireland is classified in the IFRS leaning group. André (2017) classifies Malta and Ireland as being generally aligned with IFRS and IFRS for SMEs respectively. Interestingly, other countries classified together with Malta in previous literature are, in this study, classified in cluster 1. Such different classifications result due to the different focus of the various research, with this particular study being the first to cluster accounting systems with a focus on small entities. Such a focus brings along important considerations into the equation, including the extent of relief of the administrative burden of financial reporting on small entities – entities which play an important role in the economies of the various member states. In view of this, some member states sought to maximise the benefits flowing to small entities as can be seen in the options relating to the preparation of management reports, the abridged balance sheet and the abridged profit and loss account.

Cluster 1	Cluster 2
Bulgaria	Ireland
Czech Republic	Malta
Estonia	Slovakia
Germany	
Italy	
Spain	

Table 1. Cluster Analysis

CONCLUDING NOTE

This article suggests that previous national GAAPs continue through the new national GAAPs, even following the transposition of the Accounting Directive, such that international comparability remains in doubt. Two clusters in fact result. This suggests that harmonisation has not been fully achieved perhaps to the extent originally expected, due to the numerous MSOs provided. These might be however, considered to be inevitable, as the needs and circumstances across the different member states vary.