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# CONCLUSION ON ACCOUNTING AND REPORTING

# BY TRANSNATIONAL CORPORATION

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United Nations Centre on Transnational Corporations

# Conclusions on accounting and reporting by transnational corporations

## The Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting

United Nations
New York, 1988

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# Preface

Transparency in the global activities of transnational corporations is necessary for informed decision-making by investors, employees, home and host governments. Over the years, national and international groups have been seeking to improve both the quantity and the quality of information disclosed by transnational corporations. This booklet is a contribution to this important endeavor. It is intended to serve as a guide for both the preparers and the users of financial statements indicating to them not only the items to be disclosed, but also the manner in which they are to be disclosed.

This booklet contains the results of nearly a decade of discussions and deliberations by the Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting and its predecessor group, both subsidiary bodies of the United Nations Commission on Transnational Corporations. If all their agreed conclusions on appropriate accounting and reporting procedures for transnational corporations were observed, the availability and comparability of corporate information would be considerably improved.

There is an urgent and growing need in this world of globalized financial markets for meaningful and accurate information. While large transnational corporations possess a thorough knowledge of their own operations, others such as investors, employees and governments are confronted with an overwhelming array of complex details and conflicting information.

At the present time it is almost impossible to compare the performance of transnational corporations because of different national accounting standards. For example, reported net income might differ by a factor of 25 for the same financial results depending on national accounting standards. In addition, many transnational corporations continue to be selective in the type of information they provide. Often design is more important than content. It was surprising, for instance, that a number of the 1987 annual corporate reports were completely silent about the impact of the 19 October 1987 crash on their operations.

It is my hope that this booklet by the Intergovernmental Working Group will contribute to the long-term objective of international harmonization of accounting standards. Increased transparency through greater availability and comparability of information can only bring about more stabilty in our uncertain world.

New York, September 1988

Peter Hansen
Executive Director

## EXPLANATORY NOTES

Symbols of United Nations documents are composed of capital letters combined with figures. Mention of such a symbol indicates a reference to a United Nations document.

Reference to "dollars" ($) indicates United States dollars, unless otherwise stated.

Reference to "tons" indicates metric tons, unless otherwise stated.

The term "billion" signifies a thousand million.

Annual rates of growth or change refer to annual compound rates, unless otherwise stated.

A hyphen (-) between years, e.g. 1985-1986, indicates the full period involved, including the beginning and end years; a slash (/) indicates a financial year, school year or crop year, e.g. 1985/86.

A point (.) is used to indicate decimals.

The following symbols have been used in the tables:

Two dots (..) indicate that data are not available or are not separately reported.

A dash (--) indicates that the amount is nil or negligible.

A hyphen (-) indicates that the item is not applicable.

A minus sign (-) before a number indicates a deficit or decrease, except as indicated.

Details and percentages in tables do not necessarily add to totals because of rounding.

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## Introduction

1. To understand the nature and the effects of the activities of transnational corporations, users of financial statements need to have adequate information providing a true and fair view of the performance and the situation of the enterprise as a whole and its individual member entities. An essential step in this process is to improve the availability and international comparability of information presented in the general-purpose reports of transnational corporations. For this purpose there is a need for continuing efforts to encourage international harmonization of accounting and reporting rules and standards.

2. The involvement of the United Nations Centre on Transnational Corporations in issues of accounting and reporting by transnational corporations dates back to 1975 when, following the recommendation of the Report of the Group of Eminent Persons published in 1974, the Commission on Transnational Corporations established the Group of Experts on International Standards of Accounting and Reporting. The Group, which was composed of high-level experts serving in their personal capacity, reported to the Commission in 1977 and recommended lists of minimum disclosure items for general-purpose reports by an enterprise as a whole and its individual member entities. 1/

3. By resolution 1979/44, the Economic and Social Council, acting on the recommendation of the Commission on Transnational Corporations, decided to establish an *Ad hoc* Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting composed of 34 members. On the basis of its mandate the Group decided to focus on the following activities:

(a) To review the lists of minimum items for general-purpose reporting by business enterprises, taking into account the 1977 report of its predecessor;

(b) To review materials from international accountancy bodies and other interested groups;

(c) To consider participation of all countries, in particular the developing countries, and the United Nations in the formulation and adoption of international standards of accounting and reporting;

(d) To consider further steps to be taken in the field of accounting and reporting within the scope of the work of the Commission, in particular as regards the comprehensive information system and the draft code of conduct on Transnational Corporations currently being formulated; and to improve the comparability of the information provided by transnational corporations in their reports.

4. In the report on its sixth session, 2/ the *Ad Hoc* Group presented agreed conclusions on many items to be included in minimum lists for disclosure by transnational corporations, and their individual member entities. In areas where no agreement proved possible, the different positions of delegations were recorded. The report also identified a number of subjects that required further consideration. In addition, the *Ad Hoc* Group was requested to provide comments on the proposed code of conduct. It suggested certain items of disclosure, most of which were included in the draft code of conduct.

5. By resolution 1982/67 the Economic and Social Council established the Intergovernmental Group of Experts on International Standards of Accounting and Reporting to serve as an international body for the consideration of issues of accounting and reporting falling within the scope of the work of the Commission on Transnational Corporations in order to improve the availability and comparability of information disclosed by transnational corporations. For this purpose the Group was given the work of reviewing developments in accounting and reporting, including the work of the standard-setting bodies, and establishing priorities, taking into account the needs of home and host countries, particularly those of developing countries.

6. The Group is the only intergovernmental body active in the field of accounting and reporting in which both developed and developing countries are represented. Several other international bodies working in the field of accounting and reporting (the European Economic Community, the Organisation for Economic Co-operation and Development and the International Accounting Standards Committee) and representatives of both preparers and users of financial statements (the International Chamber

of Commerce and the International Confederation of Free Trade Unions) participate in the deliberations of the Group.

7. Pursuant to its mandate, the Group has carried out several important functions. It has discussed major features of the standard-setting process at all levels and raised awareness of common elements as well as divergent approaches which might constitute obstacles to greater harmonization of accounting practices. The Group has contributed to increased understanding of accounting and reporting by transnational corporations, and the consensus achieved has served as a basis for bridging information gaps between transnational corporations and users of information. Building upon the work of its predecessor, the *Ad Hoc* Group, it has identified and examined a number of items for disclosure of financial and non-financial information by transnational corporations in the general-purpose reports of the enterprise as a whole and its individual member enterprises. These items relate to the activities of all transnational corporations, with the exception of specific issues arising for accounting and reporting by banks and insurance companies, which could be examined at a later stage.

8. Many countries, especially developing countries, have not established standard-setting bodies, and some have done so with very limited resources. The work of the Group can help these countries achieve the goals of standardization and harmonization of accounting practices, which will improve the availability and comparability of information.

9. The Group concluded that its work would be more accessible if the results thus far achieved were widely disseminated in a comprehensive and systematically structured document. For this purpose, the Group has prepared the present document to assist preparers and users of financial statements.

10. The Group has also identified a number of issues requiring further consideration, e.g., accounting and reporting issues relating to business combinations, specific industries, leases, pension costs, labour and employment, income taxes as well as accounting in highly inflationary economies. Subsequent editions of the document will incorporate the conclusions reached on such issues.

11. Part One reproduces the Group's conclusions on the main aspects of the accounting standard-setting process and the need for international

harmonization. Part Two regroups within a systematic framework all conclusions on accounting and reporting reached by the Group and its predecessor, the *Ad Hoc* Group.

## Part One

# MAIN ASPECTS OF THE PROCESS OF SETTING ACCOUNTING STANDARDS 3/

12. The Group recognized that (a) various accounting and reporting standards* had been established by legislation in a number of countries; (b) different standards had been promulgated by various governmental, intergovernmental and non-governmental bodies at the national, regional and international levels; (c) varying accounting policies had evolved over the years in response to the variety of types of business enterprise, the complexity of business transactions, and differences in social and economic systems; and (d) divergent accounting and reporting practices continued to prevail in a number of areas.

13. It was agreed that the Group should consider its role as an interested party in the standard-setting process. Accordingly, the Group should (a) serve as a forum for discussion of the needs of home and host countries for the establishment of standards of accounting and reporting; (b) act as a catalyst in the development of such standards by stimulating and encouraging the efforts of the standard-setting bodies; (c) review the work of the standard-setting bodies and offer comments with a view to meeting the needs of home and host countries; and (d) consider any relevant provisions that might arise from the implementation of particular standards.

14. The Group agreed that it would be desirable for the standard-setting bodies to take into account the results of the Group concerning harmonization of divergent accounting and reporting practices and disclosure of information to meet user needs, particularly in the developing countries. It was proposed that the Group might wish to consider the question whether standard-setting efforts should involve participation by representatives of Governments, the accountancy profession, the business community and user groups, and also the degree of that involvement,

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*The word "standards" in the context of the present report includes both legislative and non-legislative pronouncements.

including the active participation of developing countries in the standard-setting process. Some delegations were of the view that the Group should not suggest who should participate in standard-setting.

15. The Group agreed that the purpose of standard-setting should be to promote, *inter alia,* adequate disclosure of comparable information, including non-financial information, giving a true and fair view of financial position and profit and loss in the financial statements.

16. The Group noted that accounting and reporting requirements were embodied in various legal instruments in many host and home countries. Statute law could establish very detailed requirements, or simply a basic framework, or any range of intermediate positions. Those requirements might be interpreted by court decisions. Those national Governments establishing such statutory requirements recognized the need for governmental action to regulate the accounting and reporting practices of business enterprises and the need to secure enforcement for those requirements.

17. The Group noted that standards could be developed by either government or non-governmental bodies. In the latter case, the standard-setting process usually comprised the following sequential steps: (a) the identification and definition of issues; (b) research work on such issues; (c) publication of a discussion paper for consideration by interested parties; (d) issue of an exposure draft for comments by interested parties; (e) promulgation of the final standard.

18. The Group considered that there was a widespread coexistence of and complementary relationship between statutory requirements and other standards issued by standard-setting bodies, both governmental and non-governmental. The Group recognized that legislative pronouncements were enforceable by their very nature and it therefore further considered means of the enforcement of non-legislative standards. The Group recalled the importance of each country having, within the framework of its national law, an effective means of implementing the standards that were generally accepted for accounting and reporting within its system. It accepted the need for enforcement of such standards but, in view of the diversity of national legal systems and traditions, was of the opinion that differing mechanisms would be appropriate in different countries. In some countries legislation regarding the observance of those standards would be

appropriate, whereas in other countries the enforcement mechanisms could take other forms.

19. The Group agreed that the following criteria were among those used in defining the applicability of accounting and reporting standards:

(a) The concept of corporate limited liability;

(b) Public ownership of shares;

(c) Foreign ownership and/or control;

(d) Size of the entity in terms of net sales, total assets and number of employees.

20. Regarding disclosure of information in general-purpose reports, the Group agreed that it should be made available in a manner accessible to the public.

21. The Group noted that a number of countries had already established accounting and reporting standards dealing with a variety of issues, while others had yet to do so. The question arose as to what could be done to economize and facilitate standard-setting efforts, especially in the developing countries. One possibility was for representatives of countries to consult internationally on major issues of common concern, since one country's experience today was another's tomorrow. Another possibility was to provide developing countries with advisory services and technical co-operation programmes on standard setting. The Group agreed that harmonization of accounting and reporting standards should aim at improving the comparability of financial statements. An important step in defining the scope for harmonization was the comparison of standards to identify similarities and differences. The view was expressed that the comparison process could be facilitated if each standard comprised comparable elements, such as the objective(s), the concept(s), the scope of coverage, definitions of terms, criteria of applicability, bases of measurements, the accounting method(s), information disclosure and explanatory notes. However, it was pointed out that all those elements were not necessarily to be found in each standard. The Group agreed that accounting standards should comprise, where appropriate, comparable elements.

22. Given that standard setting continued to take place at the national level, the Group perceived the need for continuing efforts to promote international harmonization, while recognizing that harmonization did not necessarily imply uniformity. Issues of harmonization were of interest to home and host countries and should be the subject of multilateral consultation. The Group's consensus on those issues could contribute to the harmonization process in the interest of improved information disclosure by transnational corporations.

## Part Two

## SUBSTANTIVE ISSUES OF ACCOUNTING AND REPORTING

# I. OBJECTIVES AND PRINCIPLES OF ACCOUNTING AND REPORTING

### A. Objectives of financial statements 4/

23. The objective of financial statements is to provide information about the financial position, performance and changes in financial position of an enterprise, which is useful to a wide range of users in making decisions and is necessary for the accountability of management for resources entrusted to it. Financial statements can also provide useful information to Governments to make policy decisions.

24. The users of financial statements include present and potential investors, lenders, suppliers, employees, customers, Governments and the public and those acting on behalf of such users.

### B. Information needs 5/

25. Accounting and reporting by transnational corporations should take account of the information needs of users, particularly in home and host countries, especially in developing countries, in view of the great interest in better understanding the activities of transnational corporations and their social and economic impact. Comparability of information is an important factor in this regard.

26. Reports by transnational corporations should disclose all items which are material enough to affect evaluations or decisions by users whether or not the disclosure of such items is explicitly required.

27. Transnational corporations as a whole, regardless of their size, should be subject to general-purpose reporting requirements. The extent and nature of the information disclosed should take into account the transnational corporation's size.

28. The principle of non-discrimination between transnational corporations and national enterprises in the context of reporting requirements is recognized.

29. The costs of providing information should bear a reasonable relationship to the benefits derived therefrom. It is also necessary to take into account the need of transnational corporations to maintain business confidentiality in sensitive areas, in particular so as not to jeopardize their competitive position.

30. Disclosure of information in general-purpose reports should be made in a manner accessible to the public. Individual member enterprises should, consistent with local practice, disclose information in the language and currency of the host country.

## C. Components of financial statements 6/

31. Annual financial statements generally comprise the balance sheet, income statement, statement of allocation of net profits or net income, statement of changes in financial position and notes to the financial statements as well as any explanatory material or schedules identified as an integral part of the financial statements.

## D. Auditor's association with financial statements 7/

32. Financial statements are prepared for the purpose of enabling users to form a sound opinion of the financial position and the results of the enterprise as a whole, or the individual member enterprises, as the case might be (true and fair view requirement). Financial statements should, therefore, be comprehensive, containing all the information, whether of a financial or a non-financial nature, necessary for that purpose. The auditor,

having audited the financial statements, should express his opinion on whether or not the statements complied with established standards and met the true and fair view requirement. The auditor should give attention to both the financial and the non-financial information included in the financial statements.

33. Moreover, the auditor should satisfy himself that the report of the directors for the financial year and any other document published with the financial statements as a single set contains no information that is inconsistent with that included in the financial statements.

34. The information included in reports, other than financial statements, could equally be of a financial or a non-financial nature. Whether or not non-financial information could be audited would depend on the circumstances.

## E. Special-purpose reporting 8/

35. It is important to distinguish clearly between the functions of general-purpose and special-purpose reporting.

36. Considering the parameters which impose certain limitations on the scope of information disclosure in general-purpose reports, special-purpose reports constitute an important source of much information specifically required by user groups such as Governments, employees, trade unions and public interest organizations. Because of the particular needs of each user group, there is a wide variety of special-purpose reports each of which provides specific information required by a specific user group for a specific purpose.

37. Special-purpose reports can contain confidential and detailed information not found in general-purpose reports. The confidentiality of information should be respected, but public disclosure of such information may be permitted by mutual agreement or at the time the information ceases to be of a confidential character.

## F. Concepts underlying financial reporting

### 1. True and fair view 9/

38. Financial statements should contain adequate information giving a true and fair view.

### 2. Substance over form 10/

39. Financial accounting should emphasize the economic substance of events even though the legal form might differ from the economic substance and suggest different treatment. Where this approach is precluded by national law appropriate disclosure should be made.

### 3. Revenue recognition 11/

40. In some countries, the term "income" is used instead of "revenue". Revenue is an important component in the calculation of earnings as reflected in the formula: Revenue - Expenses + Gains - Losses = Earnings. The recognition of revenue on a consistent and appropriate basis is fundamental to the preparation of the income statement.

41. There can be uncertainties affecting recognition of revenue, as in the following cases:

(a) The consideration receivable is not determinable within reasonable limits;

(b) Costs to be incurred in producing or purchasing goods or services cannot be reasonably determined;

(c) The coagulability of the receivable resulting from a sale transaction is uncertain;

(d) There is uncertainty regarding the amounts of returnable goods.

42. Revenue should be earned as well as realized, or clearly capable of realization, before it is recognized. Revenue is considered to have been earned when the requirements concerning performance are satisfied and

collection of the invoice amount is reasonably assured. Revenue is realized when goods or services are exchanged for cash or claims to cash.

43. The following items should be disclosed:

(a) Revenue derived from the sale of goods and/or the rendering of services, as well as from the use by others of enterprise resources yielding interest, royalties and dividends;

(b) Accounting policies describing the method(s) used in recognizing revenue.

# II. CONSOLIDATED FINANCIAL STATEMENTS OF TRANSNATIONAL CORPORATIONS

## A. Concepts related to consolidation

### 1. Group enterprises 12/

44. Financial data of group enterprises should be consolidated. Exceptions should be explained in the notes to the consolidated financial statements. Consolidation is understood to involve, among other things, the application of accounting principles and practices to eliminate transactions, investments and other balances and profits - and sometimes losses - arising from transactions among group enterprises consolidated. The consolidated financial statements present financial information concerning the enterprises consolidated as if they were a single enterprise.

45. The situations in which the preparation of consolidated financial statements is required vary from country to country. Most countries require such statements, however, where a parent company owns a majority of the voting shares in another enterprise and where there is no impairment in its ability to control that enterprise. Other situations where the preparation of consolidated financial statements may be required are as follows: 13/

(a) The parent entity owns the majority of shares of another enterprise but not the majority of voting power;

(b) The parent entity exercises control over another enterprise by virtue of a provision in the memorandum of association or of a term in a contract;

(c) The parent entity has the right to appoint the majority of the members of the board of directors or the supervisory board of another enterprise;

(d) The parent entity regularly controls the voting decisions at the general meetings of shareholders of another enterprise and, in that manner, exercises *de facto* control, even though it has neither the majority of the capital nor the majority of the voting power;

(e) The parent entity exercises a dominant influence over another entity;

(f) Two or more entities are managed on a unified basis.

46. Where an enterprise is considered to have met the conditions for inclusion in the consolidation, it should be excluded only in exceptional circumstances. When an entity is excluded, the following should normally be disclosed: 14/

(a) The name of the entity concerned;

(b) The reason why the entity has not been included in the consolidation;

(c) Financial information relating to the excluded entity.

### 2. Associated enterprises 15/

47. An associated enterprise in relation to a transnational corporation is understood to mean an enterprise - other than a group enterprise - in which the transnational corporation holds a substantial interest or over whose financial or operating policies the transnational corporation exercises a significant influence. Investments in associated enterprises are normally to be accounted for by the equity method. Exceptions are to be justified and

disclosure should be made, in the notes, of the equity in net assets and net income for the period.

### 3. Accounting for foreign direct investment 16/

48. For the purpose of the present document the term "direct investment" denotes equity participation by member enterprises of a transnational corporation in a corporate enterprise over which those enterprises have control or over which they exercise significant influence. That definition covers equity participation in both foreign and domestic operations.

49. In the financial statements of the enterprise as a whole, direct investment in individual member enterprises is consolidated and thereby takes the form of the assets, liabilities, earnings and losses of the investees. Direct investment in associated enterprises, on the other hand, is accounted for in the financial statements using either the cost or the equity method. In so far as the financial statements of the individual member enterprises are concerned, direct investment is accounted for using either the cost or the equity method.

### 4. Investment in joint ventures 17/

50. For the purpose of the present document, the term "joint venture" denotes shareholdings in a business entity having the following characteristics:

(a) The entity was established by a contractual arrangement (usually in writing) whereby two or more parties (the venturers) contributed resources towards the business undertaking;

(b) The venturers have joint control over one or more activities carried out according to the terms of the arrangement and none of the individual investors is in a position to control the venture unilaterally.

51. Several methods are used to account for investment in joint venture. Current accounting practices reflect the influence of legal and economic considerations prevailing in different countries. Accounting for investment

in joint ventures requires considerable judgment in selecting an appropriate method.

### 5. Equity method 18/

52. Under the equity method, an initial investment by a transnational corporation in another enterprise is so adjusted in the consolidated financial statements of the transnational corporation as to reflect its share of the net assets of the other enterprise. The consolidated income statements reflect the transnational corporation's share of the operating results of the other enterprise.

## B. Disclosure of information concerning members of a group and associated enterprises 19/

53. The enterprise as a whole should disclose:

(a) The identity of the parent enterprise if its name is not included in the name of the group;

(b) The names of the main enterprises within the group, indicating:

(i) The percentage owned;

(ii) The geographical area or country of operations.

The exclusion of a group enterprise from consolidation should be justified and the accounting treatment of the investment in such enterprises explained.

(c) The names of main associated enterprises, indicating:

(i) The percentage owned;

(ii) The geographical area or country of operations.

The accounting treatment of such investments should be explained.

(d) The policies applied in respect of transfer pricing.

54. The individual member enterprise should disclose:

(a) The identity of the parent enterprise and of its ultimate parent, if known;

(b) The names of the main controlled and associated enterprises, indicating:

(i) The percentage owned;

(ii) The geographical area or country of operations.

The accounting treatment of such enterprises should be explained.

(c) The amount of guarantees on behalf of other members of the group and associated enterprises;

(d) The policies applied in respect of transfer pricing.

## C. Methods of consolidation 20/

55. When the underlying circumstances are similar, the accounting policies followed by all the entities in the consolidation should be the same for the purpose of preparing consolidated financial statements. Where in exceptional circumstances different policies have been followed in the consolidated financial statements for identical or similar items, that fact should be disclosed, together with the reason why a different accounting policy has been followed.

56. When, for one or more entities included in the consolidation, it has not been possible to use financial statements or data at dates which substantially coincide with those of the consolidated financial statements, this fact, the reason therefor and the periods covered by the statements or data that do not coincide, should be disclosed. Consideration should also be given to adjusting for, at least disclosing, any significant transactions or other events that have occurred during the intervening period.

57. In aggregating financial data, various adjustments may be necessary to reflect the financial position and operating results of the consolidated enterprises as if they were a single entity.

58. The carrying amount of the parent's investment in each of the subsidiary entities included in the consolidation is set off against the parent's portion of the equity in each of these entities. Any positive difference arising from this adjustment is referred to as "goodwill". Any negative difference is either applied against other assets or referred to as "negative goodwill".

59. In preparing consolidated financial statements, intercompany balances and transactions between entities included in the consolidation should be eliminated. Gains and losses included in the carrying values of assets transferred within the enterprise as a whole that are still on hand should normally be entirely eliminated; at a minimum, the parent entity's portion of such gains and losses should be eliminated. If such losses represent a permanent decline in the value of such assets, however, consideration should be given to recognizing such decline by writing down the amounts of such assets.

60. Any minority interest in the equity of consolidated entities should be separately disclosed in the consolidated balance sheet, and any minority interest in the net income or net loss of such entities should be separately disclosed in the consolidated income statement.

## III. ACCOUNTING AND REPORTING FOR BUSINESS COMBINATIONS 21/

61. For the purpose of this report, the term "business combination" denotes a linkage by way of equity interest between two or more enterprises. The linkage, which may be effected in various ways, would allow the two or more enterprises to act as a single economic entity. There is a need to develop the concepts and harmonize the accounting treatment of business combinations.

# IV. SEGMENTATION OF INFORMATION

## A. Determination of segments 22/

62. Only significant segments should be separately reported.

### 1. Industry segments

63. For the purpose of this document the term "industry" is used in the widest possible sense and refers to all sectors of economic activity. The wide variety of operations among enterprises makes it difficult to develop standard criteria on how an industry segment should be established. Each enterprise should be allowed to make its own determination, based on factors such as the nature of the products or services, the profitability, risk and growth of the products and services, the nature of the production process, the nature of markets and the enterprise's existing profit centres.

### 2. Geographical area

64. It would be both impracticable and inappropriate to prescribe uniform criteria for delineating a geographical area. Hence each enterprise should be allowed to make its own determination, based on factors such as the physical location of the operations, proximity of operations, existing conditions in each area, and the nature, degree and scale of interrelationship of the enterprise's operations in the various countries. Normally, domestic operations would constitute a separate geographical segment.

65. Only significant segments should be separately reported.

## B. Disclosure of segmented information 23/

66. For enterprises whose securities are publicly traded or that are economically significant, consideration should be given to disclosing the following financial information for both industry segments and geographical segments which are considered to be significant to the enterprise:

(a) A description of the activities of each reported industry segment and the composition of each reported geographical segment;

(b) For each reported industry and geographical segment, the following financial information:

(i) Sales or other operating revenues from customers outside the enterprise;

(ii) Sales or other operating revenues derived from other segments;

(iii) Segment result (segment result = segment revenues-segment expenses);

(iv) Segment assets employed;

(v) The basis of inter-segment pricing;

(vi) Number of employees;

(c) A reconciliation of the sum of the information on individual segments and the aggregated information included in the financial statements;

(d) Changes in identification of segments and changes in accounting practices used in reporting segment information which have a material effect on the segment information.

## V. FOREIGN CURRENCY TRANSACTIONS AND TRANSLATION 24/

67. Transactions denominated in foreign currencies are exposed to the effects of fluctuations in exchange rates. Foreign exchange risk management practices, adopted in anticipation of movements in exchange rates, are normally directed at minimizing the effects of fluctuations in foreign exchange rates. There are divergent practices in the following areas: (a) accounting for unsettled balances arising from foreign currency transactions

at the balance sheet date; (b) accounting for exchange differences; and (c) information disclosure.

68. The accounting and reporting of the results and financial position of business activities where businesses operated in a foreign currency are also exposed to the effects of fluctuations in exchange rates. Divergent practices exist in the following areas: (a) translation of foreign currency financial statements; (b) accounting treatment of translation differences; and (c) information disclosure. For translation of foreign currency financial statements, there are two approaches, namely, the net investment approach and the line-by-line approach. Under the line-by-line approach, four main methods are applied, namely, the current rate method, the monetary/non-monetary method, the temporal method and the current/non-current method.

69. The net investment approach has been developed with the following aims: (a) to produce results that are generally compatible with the effects of rate changes on cash flows of foreign businesses and their equity, and (b) to ensure that consolidated statements reflect the financial statements prior to translation.

70. Under the net investment approach, translation differences are usually taken directly to equity, leaving the financial statements of the foreign business essentially unchanged, except for the foreign currency translation. Under the line-by-line approach, the resulting translation differences are identified and dealt with in accordance with each enterprise's policy as set out in the preceding paragraph.

71. The following items should be disclosed:

(a) Methods of accounting for transactions denominated in foreign currencies;

(b) Methods of accounting for unsettled balances arising from transactions denominated in foreign currencies;

(c) Methods used in translating foreign currency financial statements.

# VI. ACCOUNTING POLICIES

## A. Disclosure of accounting policies 25/

72. Disclosure of accounting policies is essential for understanding the content of financial statements.

73. Notes to the financial statements should disclose all significant accounting policies which have been used, including overall valuation policies (for example, historical cost, application of a general purchasing power index, replacement value or any other basis). These disclosures should include in particular a description of the accounting policies concerning:

(a) Inclusion and exclusion of group enterprises in consolidation;

(b) Investments in group and associated enterprises;

(c) Intra-group transactions;

(d) Translation of accounts denominated in foreign currency;

(e) Transactions of group enterprises with associated enterprises;

(f) Criteria for the selection of geographical areas or countries reported separately;

(g) Criteria for segmentation by line of business reported separately.

## B. Selection and application of appropriate accounting policies

74. Judgment is required in selecting and applying accounting policies which, in the circumstances of the enterprise, are best suited to present a true and fair view of its financial position and the results of its operations.

75. Factors governing the selection and application of appropriate accounting policies by corporate management should include:

(a) User needs. Accounting and reporting by transnational corporations should take account of the information needs of users, particularly in home and host countries, especially in developing countries, in view of the great interest in better understanding the activities of transnational corporations and their social and economic impact;

(b) Materiality. Reports should disclose all items material enough to affect evaluations or decisions by users;

(c) Substance over form. Financial accounting should emphasize the economic substance of events even though the legal form might differ from the economic substance and suggest different treatment. Where this approach is precluded by national law, appropriate disclosure should be made;

(d) Consistency. The preparation of comparative financial statements should be based on accounting policies consistently applied andchanges in such policies and the effects thereof should be disclosed;

(e) Comparability. Many users' decisions involve choosing between alternatives, the most obvious example being that of the investment decision in which scarce resources have to be allocated among competing alternatives. Comparisons are often made between one company and another, or between the results of a company in one year and its results in some previous years. Lack of apparent comparability could be attributed to the use of various accounting methods;

(f) Prudence. The accounting concept of prudence is one of the several criteria governing the selection and application of accounting policies, in view of the uncertainties that inevitably surround many transactions. Excessive prudence could be just as unrealistic as excessive optimism in that it might, in certain circumstances, be inconsistent with a true and fair view being shown and, in particular, lead to secret or hidden reserves being created.

# VII. INFORMATION ITEMS FOR GENERAL-PURPOSE REPORTING

76. The following information items should be disclosed by (a) the enterprise as a whole; and (b) the individual member enterprise unless otherwise stated.

## A. Balance sheet and notes thereto

### 1. Property, plant and equipment 26/

#### (a) Accounting treatment including depreciation accounting

77. It is appropriate to regard property, plant and equipment as economic resources representing expected future benefits to be used up in the production of goods and/or provision of services on a continuing basis. Accordingly, it is appropriate to capitalize expenditures on property, plant and equipment. Such expenditures should include the initial cost of acquisition and post-acquisition expenditures which would extend the useful life, increase the capacity or improve the efficiency of property, plant and equipment. The amount to be capitalized should comprise the purchase price or production cost and all other expenditures necessary to put the asset in operating condition and location for use. Interest on debt could be capitalized as part of the cost of property, plant and equipment up to the time when the asset is ready for use.

78. The predominant practice in accounting is to account for property, plant and equipment on the basis of their historical cost. However, there could be instances where it would be appropriate to reflect property, plant and equipment at values different from historical cost. Those instances could be indicated by considerations such as inflation rates, specific price changes, currency revaluation and fluctuations in foreign exchange rates. In cases of permanent impairment and technological obsolescence, a write-down should be made.

79. Property, plant and equipment with limited useful lives should be depreciated. The aim of the depreciation method used should be to provide a reasonable, consistent matching of revenue and expense by systematically allocating the cost of depreciable asset over its estimated useful life. The

basis and method used in computing depreciation should be those that best reflect the underlying physical, technical and economic facts, and should be such that they could be reliably and consistently applied. Depreciation rates should be reviewed periodically and, if necessary, adjusted so that they reflect the most recent estimates of the useful lives of the respective assets, having regard to such factors as asset usage and the rate of technical and economic obsolescence, and also the most recent assessment of the net amounts expected to be recovered on their disposal.

(b) Disclosure of property, plant and equipment

80. Financial statements should disclose property, plant and equipment providing information in regard to both owned and non-owned properties shown in the accounts. Leaseholds and improvements thereto should be included under this item where they are treated as assets.

81. Disclosure concerning property, plant and equipment should be required in financial statements or the notes thereto. Disclosure should include (a) the gross carrying amounts of land and buildings, plant and equipment; (b) acquisitions, disposals, transfers, write-offs and revaluations during the year; (c) exceptional profit or loss from sales, disposals and transfers, if material; (d) depreciation for the year and accumulated depreciation; (e) the bases used in determining the gross carrying amounts or revalued amounts; (f) the depreciation methods and rates used; and (g) the extent to which property, plant and equipment have been pledged as security. Where land and buildings, plant and equipment are material in relation to total assets, an appropriate breakdown should be provided.

## 2. Investments 27/

82. The enterprise as a whole should disclose separately investments in group enterprises not consolidated, investments in associated enterprises and other long-term investment. The individual member enterprise should disclose separately investments in group enterprises, investments in associated enterprises and other long-term investments.

83. Regarding direct investment in associated enterprises, long-term investment in marketable securities and investment in joint ventures, the enterprise as a whole should disclose:

(a) The amount invested during the year;

(b) The carrying value of the investment at the end of the year;

(c) The income derived from the investment;

(d) Changes in the value of the investment;

(e) An exceptional gain or losses arising from sales of the investment, if material.

84. Significant new direct investment should be disclosed by geographical area.

85. The investing enterprise should disclose the name and host country of each of (a) the investees under its control or significant influence; and (b) its joint ventures, showing the proportion of the capital held, the amount of capital, retained earnings and reserves, and the profit or loss for the latest financial year of the undertaking concerned for which accounts had been adopted.

86. Long-term investments in marketable securities are sometimes accounted for in financial statements at their historical cost and sometimes at their market value. Marketable debt securities are currently accounted for at their historical cost, their present value or their market value.

### 3. Receivables and payables

(a) Long-term receivables 28/

87. Receivables from group enterprises not consolidated, or in the case of individual member enterprises receivables from group enterprises, receivables from associated enterprises and other long-term receivables should each appear separately.

(b) Receivables 29/

88. Accounts and notes receivable (trade), receivables from members of the board of directors, and other receivables should each be indicated.

89. Individual member enterprises should indicate receivables from group and associated enterprises separately.

90. Appropriate explanations and descriptions should be given of other receivables.

(c) Payables 30/

91. Accounts and notes payable (trade), payables to members of the board of directors, taxes on income, dividends payable, as well as other accounts payable and accrued expenses should each be shown.

92. Individual member enterprises should show payables to group and associated enterprises separately.

93. Appropriate explanations and descriptions should be given of other accounts payable and accrued expenses.

(d) Receivables and payables: members of the board of directors 31/

94. Balances receivable from or payable to directors which might otherwise be considered immaterial should be reported in the notes because of their nature.

4. Purchased goodwill 32/

95. This item should be disclosed.

5. Patents, trademarks and similar intangibles 33/

96. This item should include only expenditures incurred to acquire these intangibles. Valuations should not be included unless identified as such in those jurisdictions that permit it.

### 6. Deferred charges 34/

97. This item generally includes expenditures not recognized as a cost of operations in the period in which they are incurred but which are carried forward to be written off over a period of years. Where treated as assets, the following would each appear separately: formation expenditure, research and development and other deferred charges. Appropriate explanations and descriptions should be given of other deferred charges. This item excludes prepaid expenses reported elsewhere. When used as "other" long-term assets, an appropriate descriptive caption should be used in place of deferred charges if a material balance is carried.

### 7. Cash 35/

98. This item should show cash on hand and in banks, including time deposits due within a short period.

### 8. Inventories 36/

99. The term "inventory" denotes the aggregate of items of tangible property held (a) for sale in the ordinary course of business; (b) in the process of production for such sale, or (c) for consumption in the production of goods or services for sale, including maintenance supplies and consumables.

#### (a) Valuation of inventory cost: selection of an appropriate method

100. Different practices exist as regards the composition of inventory cost, the methods of costing inventory and the bases of inventory measurement. Thus, there is a need for harmonization in those instances where the application of different practices would limit the comparability of the financial statements.

101. Inventory cost should normally comprise the applicable expenditures and charges directly and indirectly incurred in bringing an inventory item to its existing condition and location. In some countries it is an accepted practice to include only direct expenditure and charges in inventory cost.

102. Considering that various accounting methods exist and that they are based on different assumptions about inventory movements and cost flows, in selecting a method the major objective should be to choose the one that, under the circumstances, most clearly reflects the economic reality of the situation. The overriding consideration should be that the method selected permits a true and fair view of the results of operations and the financial position of the enterprise. The method adopted should be consistently applied from period to period and adequately disclosed in the financial statements.

(b) Disclosure of inventories and of valuation policy

103. Inventories should be disclosed in the balance sheet. Where inventories are a material item, an appropriate breakdown - such as raw materials, work-in-process, finished goods, goods in transit, spare parts and supplies, and long-term contracts in progress - should be provided, and the amount for each category shown. However, where special circumstances would entail undue expense, inventories could be combined in the consolidated accounts.

104. Information should be disclosed in respect of (a) the accounting policies adopted for the purpose of inventory valuation, (b) change in inventory valuation policy that had a material effect in the current period or might have a material effect in subsequent periods, and (c) the effect of the change in inventory valuation policy.

105. Where book value of inventories determined on the basis of the weighted average price, first-in, first-out (FIFO), last-in, first-out (LIFO), or other similar methods differs materially from the market value at the balance-sheet date, the amount of the difference should be disclosed in the notes to the accounts.

106. The amount of inventories pledged as collateral for repayment of loans should be disclosed. The amount of any exceptional value adjustment(s) should be disclosed.

## 9. Prepaid expenses 37/

107. Prepaid expenses are to be disclosed separately.

10. Long-term loans and debentures 38/

108. A summary of maturity patterns, the basis of currency conversion and exchange rates used should be disclosed. The individual member enterprise should separately disclose loans and debentures from group and associated enterprises.

11. Short-term loans and overdrafts 39/

109. The individual member enterprise should separately disclose loans and debentures from group and associated enterprises.

12. Deferred income 40/

110. This item should be disclosed.

13. Provisions 41/

111. Deferred taxes, provisions for pensions and other provisions should each be indicated separately. Appropriate explanations and descriptions should be given of other provisions.

112. Deferred taxes are amounts provided for taxes in respect of the current and previous years' results which are expected to become payable in future periods. The amount reflects the fact that the periods in which some items of revenue and expense are recognized for tax purposes do not coincide with the periods in which they are included in accounting income.

14. Owners' interest 42/

113. A description and quantification of each component element should be provided, such as, if any, different classes of shares and other forms of owners' interest, capital paid in excess of par, revaluation surplus, reserves and retained earnings. Movements during the accounting period should be indicated.

15. Restricted assets and secured liabilities 43/

114. Where assets are restricted or pledged, or liabilities secured, an indication in summary form should be provided.

### 16. Pension plans and similar financial commitments 44/

115. Wherever an enterprise as a whole or an individual member enterprise has its own pension plan or where an individual member enterprise participates in a group pension plan, a general description of benefits, financial obligations and investment of funds should be provided. Financial commitments not shown in the balance sheet would in any case be disclosed.

### 17. Leases 45/

116. Leases not reflected in fixed assets and other long-term commitments should be appropriately described and quantified.

### 18. Contingent liabilities and assets 46/

117. Accounting and reporting of contingent liabilities and assets should be based on the concept of prudence in respect of a contingent asset, and on the degree of the probability of payment in respect of a contingent liability.

(a) Contingent liability. A condition or situation existing at the balance-sheet date that may or may not result in loss or expenditure depending on the outcome of one or more uncertain future events. A contingent liability is disclosed in the notes to the extent that it has not been accrued by a charge in the income statement, unless the possibility of a loss is remote. Contingent liabilities resulting from specific legal obligations undertaken by the enterprise, such as guarantees or discounted bills of exchange, are disclosed in the notes to the financial statements, even though it is unlikely that a loss to the enterprise will occur.

(b) Contingent asset. A condition or situation existing at the balance-sheet date that may or may not result in a gain depending on the outcome of one or more uncertain future events. A contingent asset is disclosed in the notes if it is probable that the gain will be realized.

### 19. Contracts for future capital expenditure 47/

118. Contracts for future capital expenditure should be quantified and disclosed.

## 20. Events after balance sheet date 48/

119. Material events that have occurred after the balance-sheet date should be quantified and disclosed.

## 21. Movements in certain assets 49/

120. There is a need for disclosure of information concerning movements in certain assets, namely, (a) land and buildings; (b) plant and equipment; (c) assets under construction; (d) long-term investments; (e) long-term receivables; (f) purchased goodwill; (g) patents, trade marks and similar intangibles; and (h) deferred charges of a long-term nature. For disclosure under a, b, c and d see paragraphs 81-86 above. Concerning e, f, g and h information should be disclosed in respect of opening balance (gross amounts before depreciation) acquisitions, disposals, transfers, write-offs, revaluations/adjustments and closing balance.

## 22. Reserve accounting, including hidden reserves (excluding banks and insurance companies) 50/

121. The term "reserves" is not applied universally: sometimes the term is used to describe or refer to valuation accounts, such as accumulated depreciation and allowances for uncollectible receivables, or to estimated liabilities, such as the amounts set aside by way of provisions for product warranties. Such usages should be avoided and consideration of reserve accounting should be confined to items which would normally be considered to be components of equity. Hidden reserves are created when there is a material understatement of assets, or an overstatement of liabilities. The creation of such reserves adversely affects the ability to show a true and fair view of the financial position as at the end of the accounting period, and results of operations for the period.

122. Reserves should not be used to avoid charges to operations. For example, it is inappropriate to charge to a reserve a probable loss which could be reasonably estimated. Such amounts should be charged to the profit and loss account of the current period. That would apply whether the reserve was created voluntarily or pursuant to legal requirements, and irrespective of whether it was established, *inter alia*, from accumulated earnings (revenue reserves) or from contributed capital.

123. The amounts arising from balance sheet recognition of unrealized increases in values are sometimes included in equity. Such amounts might occur, for example, upon the revaluation of fixed assets. Likewise, translation differences arising upon translation of a consolidated subsidiary's financial statements denominated in a foreign currency might be included in equity. Normally, the inclusion of those amounts in equity is appropriate before accounting recognition and measurement takes place based on transactions and events external to the enterprise, such as the disposal of a fixed asset.

124. Disclosure of information on reserves, as well as movements in each reserve, is necessary for the meaningful interpretation of an enterprise's financial statements. In that regard, the information provided should include the opening balance, changes during the period, the closing balance and the sources of changes.

## B. Income statement

### 1. Sales 51/

125. The amount reported should be a net figure, that is, the amounts derived from the sales of products and provision of services falling within the enterprise's ordinary activities after deduction of sales rebates, value-added taxes and other taxes directly linked to turnover.

### 2. Operating results 52/

126. Operating results should be disclosed so as to show sales for the period and either (a) cost of sales and operating expenses, separately, or (b) the net change in inventories, own production capitalized, raw materials and consumables, wages, salaries and related costs, depreciation and amortization and other operating earnings and expenses.

### 3. Interest and investment income 53/

127. This information should be separately disclosed.

4. Share in the net income (loss) of associated enterprises

128. The enterprise as a whole and the individual member enterprises should disclose its share in net income (loss) of associated enterprises. Reference is made to the equity method of accounting for investments in associated enterprises (see paras. 47 and 52 above).

5. Non-operating gains and losses 54/

129. Accounting for non-operating or extraordinary/unusual gains and losses should be based on the "all inclusive" concept of profit for the following reasons:

(a) Inclusion and separate disclosure of non-operating or extraordinary/unusual items permit the profit and loss account for the year to give a comprehensive view of a company's profitability;

(b) By segregating non-operating or extraordinary/unusual items for separate disclosure, the current operating profit can be shown as an element of the all-inclusive profit for the financial year;

(c) Exclusion, being a matter of subjective judgment, can lead to variations and to a loss of comparability between the reported results of companies;

(d) Exclusion can result in non-operating or extraordinary/unusual items being overlooked in any consideration of results over a series of years.

130. Non-operating or extraordinary/unusual gains and losses should be disclosed. The nature and amount of each item, if material, should be disclosed in the notes to the financial statements.

6. Interest expense 55/

131. This information should be separately disclosed. Interest expense should include all amounts that are economically the equivalent of interest, for example, premiums payable on repayment of a loan.

7. Depreciation, depletion and amortization 56/

132. It is necessary to account for (a) depreciation, especially for the use, obsolescence, wear and tear of buildings, plant and equipment; (b) the depletion of natural resources; and (c) the amortization of intangibles.

133. Disclosure should be made in respect of charges for:

(a) Depreciation of buildings, plant and equipment;

(b) Depletion of natural resources;

(c) Amortization of intangibles.

8. Taxes on income 57/

134. This item should be separately disclosed.

9. Unusual charges and credits 58/

135. Many items are included in this category, such as:

(a) Adjustments arising out of asset revaluation, where permitted;

(b) Gains or losses on sales of fixed assets;

(c) Previous years' items.

136. Items in this category should be disclosed. The nature of each item, if material, should be explained in the notes to the financial statements.

10. Inventories 59/

137. The income statement of the period should be charged with the amount of inventories sold or used (unless allocated to other asset accounts) and with the amount of any write-down to realizable value.

### 11. Employment costs 60/

138. Different components of employment costs should be disclosed separately, as follows:

(a) Wages, salaries and similar payments, including overtime to employees;

(b) Pension costs;

(c) Costs of other employee benefits.

### 12. Net income 61/

139. This item should be disclosed.

140. The enterprise as a whole should disclose separately minority interest in net income of group enterprises consolidated and its share in net income (loss) of associated enterprises. Reference is made to the equity method of accounting for investments in associated enterprises.

### 13. Research and development 62/

141. Research and developments costs are incurred by enterprises in anticipation of benefits expected in the future. The anticipated benefits may or may not materialize, may be tangible or intangible and may or may not have commercial value. Furthermore, the costs and benefits of research and development activities may not arise in the same accounting period.

142. A number of questions arise, including for example the following:

(a) What are the elements comprising research and development costs?

(b) Should research and development costs be charged as an expense of the period in which they are incurred?

(c) Under what circumstances may research and development costs be capitalized?

(d) What basis should be used to amortize research and development costs?

(e) What basis should be used for allocating research and development costs to subsidiaries and affiliates?

(f) What items of information should be disclosed?

143. The following cost elements associated with research and development activities should be disclosed:

(a) Salaries, wages and other related costs of personnel engaged in research and development activities;

(b) Costs of materials and services consumed in research and development activities;

(c) Depreciation of equipment and facilities to the extent that they were used for research and development activities;

(d) Overhead costs related to research and development activities;

(e) Other costs related to research and development activities, such as the amortization of patents and licenses.

144. The accounting policies to be followed with regard to research and development should have regard to fundamental accounting concepts, such as accrual and prudence. It is a corollary of those concepts that expenditure should be written off in the period in which it is incurred unless its relationship to the revenue of a future period can be established with reasonable certainty.

145. It is recognized that research and development costs might be capitalized if all the following criteria were satisfied:

(a) The product or process is clearly defined and the costs attributable to the product or process can be separately and clearly identified:

(b) The technical feasibility of the product or process has been demonstrated;

(c) There is a clear indication of a future market for the product or process or, if it was to be used internally rather than sold, its usefulness to the enterprise can be demonstrated;

(d) The management of the enterprise has indicated its intention to produce and market, or use, the product or process;

(e) Adequate resources exist, or are reasonably expected to be available, to complete the project and market or use the product or process.

146. The following disclosures should be made in regard to research and development activities:

(a) The accounting policies adopted as regards research and development costs;

(b) Research and development costs charged as an expense for the current period, as a specific item;

(c) The basis used to amortize deferred research and development costs;

(d) The movements of the unamortized deferred research and development costs, including:

(i) The total amount of research and development costs incurred during the current period, as a specific item;

(ii) Research and development costs of the current period deferred for amortization over future periods;

(iii) The amount of deferred research and development costs amortized and charged to expense for the current period;

(iv) The balance in the account of the unamortized deferred research and development costs at the end of the period;

(e) If research and development costs were allocated to subsidiaries and affiliates, the basis for such allocation;

(f) An indication of activities in the field of research and development during the reporting period.

147. Reference is made to the following statement:

The allocation of the costs of research and development activities to accounting periods is determined by their relationship to the expected future benefits to be derived from these activities. In most cases there is little, if any, direct relationship between the amount of current research and development costs and future benefits because the amount of such benefits, and the periods over which they will be received, are usually too uncertain. Research and development costs are therefore usually charged to expense in the period in which they are incurred. If it can be demonstrated, however, that the produce or process is technically and commercially feasible and that the enterprise has adequate resources to enable the product or process to be marketed, the uncertainties referred to [in the preceding paragraph] may be significantly reduced. In such circumstances, it may be appropriate to defer the costs of development activities to future periods. Development costs previously written off are not reinstated because they were incurred at a time when the technical and commercial feasibility of the project was too uncertain to establish a relationship with future benefits and that they were therefore proper charges to those past periods. 63/

## C. Statement of allocation of net profits or net income 64/

148. This statement should disclose the following elements:

(a) The balance of retained income brought forward from the previous year;

(b) The net income of the current year;

(c) Transfers to and from other reserves (including those required by national legislation);

(d) Dividends or similar attribution to the owners of the enterprise or group (subdivided by type);

(e) Any part of the net income payable to members of the board or others;

(f) The balance retained and carried forward to the next year.

149. The attribution of a current year's loss should be accounted for in a similar way.

## D. The statement of changes in financial position 65/

150. The statement of changes in financial position (also known as statement of sources and uses of funds) should be an integral part of the financial statements.

151. The nature and the purpose of the statement are to summarize the flow of funds during a period showing information about financial resources provided from operations and other sources and the uses made of those financial resources. The statement may also include other items which do not directly affect cash or working capital.

152. The statement should show separately significant elements of:

(a) Internally generated funds;

(b) Funds obtained from external sources;

(c) The uses to which those funds have been applied.

## E. Other information items for general-purpose reporting

### 1. Value-added 66/

153. Value-added arising from the operations of business enterprises should be disclosed. It should normally be derived from:

(a) Sales revenue less costs of material and services purchased from outside suppliers, and excise duty;

(b) Share of profits earned by or received from associated companies;

(c) Investment income;

(d) Surplus on realization of investments;

(e) Extraordinary items;

(f) Exchange gain or loss.

154. Information should be provided in respect of the distribution of value added to different contributors, such as employees and providers of capital. Value added retained in the business as represented by depreciation and retained earnings should be disclosed.

### 2. Organizational structure 67/

155. In regard to the ultimate parent, the names of members of the board of directors and, where applicable, the supervisory board, together with a description of the directorships or other senior positions held in enterprises within or outside the group should be disclosed. In cases where such disclosure would be impracticable because of its volume, it may be made available upon request.

156. The individual member enterprise should disclose:

(a) Names of members of board of directors and, where applicable, the supervisory board, together with a description of the directorships or other senior positions held in enterprises within or outside the group;

(b) Names of registered principal owners or shareholders, their nationality and the percentage owned. It is realized that this information may not be obtainable in the case of bearer shares.

### 3. Transfer pricing policies 68/

157. In respect of intra-group transactions and transactions with associated enterprises, the enterprise as a whole should disclose in its financial statements the policies followed with regard to determining the

prices for such transactions. In particular, it should indicate whether such transactions had been made on the basis of market prices or, in the absence of such prices, other methods which should be described. Individual member enterprises in the group should also disclose the volume of such transactions, either as aggregate amounts or in terms of appropriate proportions, as well as the amounts or appropriate proportions of outstanding items in so far as those disclosures are required to present a true and fair view. Those aspects should be verified by auditors.

### 4. Related party transactions 69/

158. For the purpose of the present document, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over that party in making financial and operating decisions, or if the parties share a common parent. Within a group of enterprises, related party transactions are a common feature but, because of the possibility that there could be a conflict of interest, such transactions may give rise to concern. Related party transactions are not or cannot always be carried out under conditions of competitive free-market dealings.

159. Users of financial statements need to have sufficient information to be able to assess the degree to which an enterprise's results of operations and financial position might have been affected by transactions with related parties. Disclosure of details of particular transactions with individual related parties would frequently be too voluminous to be easily understood. Accordingly, information would usually be most useful if aggregated by type of transaction and nature of relationship to provide, for example, total sales to related companies or total loans made to directors. On the other hand, disclosure on an individual basis might be more informative when there were significant transactions with specific related parties.

160. With respect to related party transactions, the enterprise as a whole should disclose in its financial statements the policies followed in regard to determining the prices for such transactions. In particular, it should indicate whether such transactions had been made on the basis of market price or, in the absence of such prices, other methods, which should be described. Individual enterprises in a group should describe their relationship(s) with related parties and the type(s) of transactions with those parties.

161. The following are examples of situations where related party transactions may lead to disclosures by a reporting enterprise in the period which they affect: purchases or sales of goods, purchases or sales of property and other assets, rendering or receiving of services, agency arrangements, leasing arrangements, transfer of technology, fund transfers, guarantees, collaterals. The volume of such transactions should be disclosed, either as aggregate amounts or in terms of appropriate proportions, as should the amounts or proportions of outstanding items in so far as those disclosures are required to present a true and fair view.

5. Labour and employment (other than employment costs) 70/

162. The enterprise as a whole should provide a description of (a) general corporate policy, if any, regarding the recognition of trade unions, and (b) any other general corporate labour relations policies; and disclose the average number of employees showing:

(a) Total employment;

(b) Breakdown by geographical area or country, as appropriate;

(c) Breakdown by line of business, in so far as practicable.

163. The individual member enterprise should disclose the following items:

(a) Number of employees as at year-end and annual average;

(b) Summary description of training programmes and the approximate related expenditures.

6. Transfer of technology 71/

164. For the purpose of the present document, the term "transfer of technology" denotes the transfer of systematic knowledge, with or without transfer of capital goods, for the manufacture of a product, for the application of a process or for the rendering of a service and does not extend to transactions involving the mere sale or the mere lease of goods. In the consolidated financial statements of the enterprise as a whole, items related

to transfer of technology to individual member enterprises are eliminated in the consolidation process.

165. Accounting for the costs of technology transfers should be based on the concept of matching cost and revenue, according to which the allocation of costs to accounting periods should be determined by their relationship to the expected future benefits to be derived.

166. Costs of technology transfers that result in the acquisition of intangible assets such as patents, trade marks, franchises, copyrights and secret processes, should be capitalized and amortized.

167. Costs of technology transfers resulting in the acquisition of tangible assets which can be segregated for the purpose of accounting, from intangible assets should be capitalized and amortized. Costs of technology transfers, including both tangible and intangible items which cannot be segregated, should be capitalized and amortized as one asset.

168. Costs of technology transfers that represent expenditures for management, technical, marketing and training services should be expensed in the period in which they arise, unless their relationship to the revenue of a future period can be established with reasonable certainty.

169. Revenue derived from transfers of technology should be recognized when all material conditions of the sale have been substantially performed and an exchange has taken place.

170. The following items should be disclosed:

(a) Costs of technology transfers capitalized during the year;

(b) Bases for amortizing the costs of technology transfers;

(c) Costs expensed on and revenue derived from transfers of technology during the year, if necessary, in order to give a true and fair view;

(d) Policies pertaining to intragroup pricing of transfers of technology.

### 7. Subsidies granted by governments 72/

171. Information concerning government grants and assistance to business enterprises should be disclosed and include the following:

(a) The accounting policy adopted for government grants, including the methods of presentation adopted in the financial statements;

(b) The nature and extent of government grants recognized in the financial statements and an indication of other forms of government assistance from which the enterprise has directly benefited;

(c) Unfulfilled conditions and other contingencies attaching to government assistance that has been recognized;

(d) Identification of significant project(s) or part of a project for which government grant(s) has been given;

(e) Any other information material enough to be disclosed.

172. Reference is made to the following accounting treatment:

(a) Government grants, including non-monetary grants at fair value, should not be recognized until there is reasonable assurance that the enterprise will comply with the conditions attaching to them, and that the grants will be received. They should not be credited directly to shareholders' interests;

(b) Government grants should be recognized in the income statement over the periods necessary to match them with the related costs which they are intended to compensate, on a systematic basis;

(c) Government grants related to assets, including non-monetary grants at fair value, should be presented in the balance sheet either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset;

(d) A government grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the enterprise with no further related costs should be recognized in the income statement of the period in which it becomes receivable, as an unusual item if appropriate;

(e) A government grant that becomes repayable should be accounted for as a revision to an accounting estimate. Repayment of a grant related to income should be applied first against any unamortized deferred credit set up in respect of the grant. To the extent that the repayment exceeds any such deferred credit, or where no deferred credit exists, the repayment should be charged immediately to income. Repayment of a grant related to an asset should be recorded by increasing the carrying amount of the asset or reducing the deferred income balance by the amount repayable. The cumulative additional depreciation that would have been charged to date in the absence of the grant should be charged immediately to income. 73/

8. Environmental measures 74

173. The individual member enterprise should provide a description of types of major or special environmental measures carried out, together with cost data where available.

9. Investment programme 75/

174. The enterprise as a whole should provide a description of announced future capital expenditures.

175. The individual member enterprise should provide:

(a) A description of announced future capital expenditures;

(b) A description of main projects, including their cost, broken down by line of business in so far as practicable;

(c) A description of announced mergers and take-overs, including related payments or other considerations.

## Notes and references

1/ E/C.10/33.

2/ E/C.10/1982/8/Rev.1.

3/ See E/C.10/1984/9, paras. 9-13, 17-18; E/C.10/1985/12 paras. 11-12; E/C.10/1986/14, paras. 20-22; E/C.10/1987/6, para. 7.

4/ E/C.10/1988/6, para. 36.

5/ E/C.10/1982/8/Rev.1, paras. 13-16; annex III, paras. 2, 4, 166, 291; E/C.10/1984/9, para. 18.

6/ E/C.10/1982/8/Rev.1, para. 10.

7/ E/C.10/1986/14, paras. 53-55.

8/ E/C.10/33, paras. 61-90.

9/ E/C.10/1982/8/Rev.1, Annex III para. 9.

10/ *Ibid*, para. 8.

11/ E/C.10/1987/6, paras. 19-21, 23.

12/ E/C.10/1982/8/Rev.1, annex III, para. 18.

13/ E/C.10/1988/6, para. 16.

14/ *Ibid.*, para. 17.

15/ E/C.10/1982/8/Rev.1, Annex III, para.21.

16/ E/C.10/1986/14, paras. 26-28.

17/ *Ibid.*, paras. 31-32.

19/ *Ibid.*, paras. 130, 275.

20/ E/C.10/1988/6, paras. 18-23.

21/ E/C.10/1987/6, para. 10.

22/ E/C.10/1988/6, paras 25 and 28-30.

23/ E/C.10/1988/6, para. 31.

24/ E/C.10/1985/12, paras. 15-20.

25/ E/C.10/1982/8/Rev.1, annex III, paras. 127, 129, 271, 274; E/C.10/1984/9, para. 20; E/C.10/1985/12, para. 14.

26/ E/C.10/1986/14, paras. 48-51; E/C.10/1982/8/Rev. 1, annex III, para. 28.

27/ E/C.10/1986/14, paras. 33-35.

28/ E/C.10/1982/8/Rev.1, annex III, paras. 34, 177.

29/ *Ibid.*, paras. 45, 46, 189-191.

30/ *Ibid.*, paras. 53-54, 200-202.

31/ *Ibid.*, paras. 65, 209.

32/ *Ibid.*, paras. 35, 178.

33/ *Ibid.*, paras. 36, 179.

34/ *Ibid.*, paras. 38-41, 182-185.

35/ *Ibid.*, paras. 42, 186.

36/ E/C.10/1987/6, paras. 26-32.

37/ E/C.10/1982/8/Rev.1, annex III, paras. 48, 193.

38/ *Ibid.*, paras. 50, 195-196.

39/ *Ibid.*, para. 198.

40/ *Ibid.*, paras. 56, 204.

41/ *Ibid.*, paras. 57-58, 205-206.

42/ *Ibid.*, paras. 60-61, 207-208.

43/ *Ibid.*, paras. 66, 210.

44/ *Ibid.*, paras. 67, 213.

45/ *Ibid.*, paras. 68, 214.

46/ *Ibid.*, paras. 71, 217; E/C.10/1983/8, para. 26.

47/ E/C.10/1982/8/Rev.1, annex III, paras. 75, 221.

48/ *Ibid.*, paras. 76, 222.

49/ E/C.10/1984/9, paras. 31-32.

50/ E/C.10/1985/12, paras. 32-37.

51/ E/C.10/1982/8/Rev.1, annex III, paras. 81, 227.

52/ *Ibid.*, paras. 84, 230.

53/ *Ibid.*, paras. 86, 232.

54/ E/C.10/1987/6, paras. 22-23.

55/ E/C.10/1982/8/Rev.I, annex III, paras. 91, 93, 237, 239.

56/ *Ibid.*, paras. 88-89, 234-235.

57/ *Ibid.*, paras. 94, 240.

58/ *Ibid.*, paras. 95-96, 241-242.

59/ E/C.10/1987/6, para. 32.

60/ E/C.10/1982/8/Rev.1, annex III, paras. 104, 249.

61/ *Ibid.*, paras. 87, 99, 233, 244.

62/ E/C.10/1985/12, paras. 24-31.

63/ *Accounting for Research and Development Activities*, IAS 9, IASC July 1978, paras. 9-10.

64/ E/C.10/1982/8/Rev.1, annex III, paras. 117-118, 262-263.

65/ *Ibid.*, paras. 120-123, 265-268.

66/ E/C.10/1984/9, paras. 36-38.

67/ E/C.10/1982/8/Rev.1, annex III, paras. 155, 299.

68/ E/C.10/1984/9, para. 40.

69/ E/C.10/1986/14, paras. 37-39.

70/ E/C.10/1982/8/Rev.1, annex III, paras. 142-143, 294.

71/ E/C.10/1986/14, paras. 42-45.

72/ E/C.10/1984/9, paras. 34-35.

73/ *Accounting for Government Grants and Disclosure of Government Assistance*, IAS 20, IASC, April 1983, paras. 37-41.

74/ E/C.10/1982/8/Rev.1, annex III, para. 303.

75/ *Ibid.*, paras. 149, 298.

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