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Centre on Transnational Corporations

# TECHNICAL PAPERS:

# INTERNATIONAL STANDARDS OF ACCOUNTING AND REPORTING FOR TRANSNATIONAL CORPORATIONS

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# INTERNATIONAL STANDARDS OF ACCOUNTING AND REPORTING FOR TRANSNATIONAL CORPORATIONS

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## 2. INTERNATIONAL STANDARDS OF ACCOUNTING AND REPORTING



Annexes

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## PREFACE

The Commission on Transnational Corporations, at its first session from 17 to 28 March 1975, recommended the establishment of an Expert Group on international standards of accounting and reporting to explore the possibility of working out standard forms for the presentation of information by transnational corporations. 1/ The recommendation was approved by the Economic and Social Council at its fifty-ninth session in July 1975. 2/

As background material to facilitate the discussions at the first session of the Group of Experts, the Centre on Transnational Corporations prepared three papers, as follows:

- "Towards international standards of accounting and reporting for transnational corporations" (E/C.10/AC.1/2);

- "International standards of accounting and reporting" (E/C.10/AC.1/3);

- "Some aspects of corporate accounting and reporting of special interest to developing host countries" (E/C.10/AC.1/4).

Because of the wide interest in this matter, these papers have been collected in the present publication.

The first paper reviews briefly the existing state of corporate reporting and identifies significant gaps and information needs, especially from the point of view of the international community as a whole. In a concluding section it presents for the Group's consideration a possible minimum list of items of financial and non-financial information which transnational corporations could disclose in their reports, and suggests possible working arrangements for the Group.

The second paper reviews current accounting and reporting practices of corporations, on the basis chiefly of detailed studies in 46 countries. It also describes the ongoing efforts to achieve standardization of general-purpose financial statements at the national, regional and international levels. In a concluding section, it reviews a number of issues and problems concerning the standardization of accounting.

The third paper examines current reporting practices of transnational corporations or their subsidiaries in developing countries in such selected areas as foreign exchange transactions, local employment, manpower training, wage and salary payments, royalties, interest on intercompany loans and the allocation of administrative expenses, and considers how reporting in these areas might be improved.

Detailed materials pertaining to the respective papers are presented in the annexes to each one.

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1/ Official Records of the Economic and Social Council, Fifty-ninth Session, Supplement No. 12 (E/5655).

2/ Official Records of the Economic and Social Council, Fifty-ninth Session, Supplement No. 1 (E/5740), Decision 114 (LIX).

# 1. TOWARDS INTERNATIONAL STANDARDS OF ACCOUNTING AND REPORTING FOR TRANSNATIONAL CORPORATIONS*

## INTRODUCTION

1. The dramatic growth and geographical spread of transnational corporations in the past quarter of a century has evoked widespread public interest in their operations. A thorough analysis of these operations and their international and national impact is, however, hampered by the paucity of information in usable form on many aspects of these corporations' activities.

2. The principal publicly available sources of information are the corporate reports - or general-purpose financial statements - issued once a year in accordance with statutory or similar requirements. These statements are designed mainly for reporting to shareholders and creditors and they focus on information relative to the corporation's financial position and the financial results of its operations. As a rule, non-financial information, such as that relating to employment and environmental aspects, is not extensively reported. Information of this kind may be of special pertinence from the viewpoint of public interest or international concern.

3. Nor do corporate reports usually contain much information on the transnational or world-wide activities of corporations in various industrial sectors and geographic regions. While some of the details of such information may be regarded as confidential, the desirability of fuller disclosure than is the practice at present has been increasingly voiced in many quarters.

4. Even general financial statements are issued in various forms, and the accounting principles and practices on which they are based vary from country to country and company to company. Their lack of comparability limits the usefulness of these reports for the purpose of any over-all appraisal of transnational corporation activities. The Group of Eminent Persons appointed by the Secretary-General of the United Nations in 1973, after emphasizing the pivotal importance of information, advocated the formulation of an "international, comparable system of standardized accounting and reporting". 1/ To this end, the Group recommended "that an expert group on international accounting standards should be convened under the auspices of the Commission" 2/ on Transnational Corporations.

5. The Commission on Transnational Corporations, at its first session from 17 to 28 March 1975, agreed that an expert group should be established. 3/ At its second session, from 1 to 12 March 1976, the Commission stressed the importance of moving ahead speedily with the establishment of standards for developing and collecting comparable information and decided that the proposed Group of Experts on International Standards of Accounting and Reporting should meet in 1976. 4/

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* Originally issued as document E/C.10/AC.1/2, dated 28 July 1976.

1/ The Impact of Multinational Corporations on Development and on International Relations (United Nations publication, Sales No. E.74.II.A.5), p. 95.

2/ Ibid.

3/ Official Records of the Economic and Social Council, Fifty-ninth Session, Supplement No. 12 (E/5655).

4/ Ibid., Sixty-first Session, Supplement No. 5 (E/5782).

6. The Commission also suggested that the Centre, in preparing a feasibility study on the subject of availability of information, might consult the Expert Group as necessary. 5/ In pursuance of the Commission's decision, the Secretary-General appointed the Group of Experts and invited the Group:

- to review the existing practice of reporting by transnational corporations and reporting requirements in different countries;

- to identify gaps in information in existing corporate reporting and to examine the feasibility of various proposals for improved reporting;

- to recommend a minimum list of items, together with their definitions, that should be included in reports by transnational corporations and their affiliates, taking into account the recommendations of various groups concerned with the subject matter.

7. In formulating the above terms of reference for the Group, it was recognized that the establishment and implementation of a standardized accounting and reporting system would be a lengthy process and that a step-by-step approach would be necessary. The elaboration of a minimum list of items which transnational corporations should disclose in their reports is viewed as a first step in the process. As envisaged by the Group of Eminent Persons, transnational corporations might include such items as additional data or issue a supplement to their annual reports which would continue to be guided mainly by national requirements. As experience was gained, however, the list and the international standards would be harmonized increasingly with national standards and normal corporate practices.

8. It is clear that even with this limited first objective, the Group will have to deal with a broad range of issues relating to the nature and purpose of the information needed, the degree of detail and the form in which the information might be collected and disclosed, and to methods of standardization and harmonization. Such reporting could include both financial and non-financial items. In view of the complexity of the task, and the need to gain wide acceptance for the Group's findings, the Group was established at the highest level, drawing upon personalities possessing not only experience and expertise in the production, use or scrutiny of corporate accounting and reporting, but also the skill and wisdom necessary for delicate international consultation and harmonization.

9. In order to assist the Group in its task, three papers are being submitted as an aid to discussion. The present paper reviews briefly the existing state of corporate reporting and identifies significant gaps and information needs, especially from the point of view of the international community as a whole. In a concluding section it presents for the Group's consideration a possible minimum list of items of financial and non-financial information which transnational corporations could disclose in their reports, and suggests possible working arrangements for the Group.

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5/ *Ibid.*, para. 22.

10. The second paper, entitled "International standards of accounting and reporting" (E/C.10/AC.1/3), reviews current accounting and reporting practices of corporations, on the basis chiefly of detailed studies in 46 countries. It also describes the ongoing efforts to achieve standardization of general purpose financial statements at the national, regional and international levels. In a concluding section, it reviews a number of issues and problems concerning the standardization of accounting. Detailed background information on current reporting practices and standardization efforts is presented in nine annexes to the paper.

11. The third paper, entitled "Some aspects of corporate accounting and reporting of special interest to developing host countries" (E/C.10/AC.1/4), examines current reporting practices of transnational corporations or their subsidiaries in developing countries in such selected areas as foreign exchange transactions, local employment, manpower training, wage and salary payments, royalties, interest on inter-company loans and the allocation of administrative expenses, and considers how reporting in these areas might be improved.

## I. MAIN FEATURES OF REPORTING PRACTICES

12. Transnational corporations are subject to the same basic reporting requirements as domestic corporations in their home countries. But national laws and regulations, or accepted professional accounting and reporting standards, may require them to present certain additional statements or items of information. Their foreign subsidiaries for their part must meet the reporting requirements of their host countries.

13. Corporations generally issue two principal types of reports: one available to the public and the other confidential. The most basic example of the first type is the annual report; containing general purpose financial statements. Other publicly available information may include ad hoc releases and specially prepared materials which may be made generally available to interested parties or supplied upon request. However, much of the information for internal corporate use, and many reports to government agencies, are confidential in nature. A notable example of a confidential report is the tax return. Some of the information submitted to government agencies may be aggregated and published in official surveys or statistical compilations. Results of special government investigations of a given corporation may also become public knowledge, especially when legal action is involved.

### A. General purpose financial statements

14. General purpose financial statements usually consist of a director's report, balance sheet, a statement of income or profit and loss account, and notes to these. Recently, a few countries have added a source and use of funds statement to the above. The issuance of these statements, which are designed mainly for reporting to shareholders and creditors, is in general required by law. In most countries the law lays down minimum reporting requirements, but corporations are free to disclose additional information. However, many companies do not go beyond the minimum requirements. Many transnational corporations issue two kinds of general purpose financial statement: a report on the enterprise as a whole, and reports by individual members of the enterprise group.

#### 1. Reports on the enterprise as a whole

15. In reports on the enterprise as a whole, the financial statements of all the units of the transnational corporation group are consolidated, with certain exceptions. In the preparation of consolidated statements, intercompany transactions and balances are eliminated. The presentation of consolidated or group statements is not mandatory in all the home countries of transnational corporations, but in recent years it has become an increasingly common practice. Consolidated statements may also be prepared for a limited number of units within a transnational corporation group, such as all the units located in a given country or those established in a group of countries. The consolidation procedure in these cases is similar to that employed in the preparation of statements on the enterprise as a whole.

16. Consolidated statements vary in coverage, depending on the criteria used for the inclusion of subsidiaries. In some countries only wholly or majority-owned subsidiaries may be included, while in others minority-owned subsidiaries may be added if the parent has effective control. The definitions and principles of consolidation are not always disclosed. Consolidated statements are designed to provide a general picture of the scope of the transnational corporation's global assets and liabilities and of its transactions, but their comparability and usefulness is limited by differences in coverage and in the accounting principles used in their presentation.

### 2. Reports by individual members of an enterprise group

17. Financial statements may be issued publicly for the parent company alone. These may be annexed to the consolidated statement, where it exists. Foreign subsidiaries, whether wholly or majority-owned, also issue general purpose financial statements in accordance with the statutory requirements of the host country. In such individual company statements, intercompany transactions and balances are included but are not always shown under separate headings.

## B. Confidential reports to Governments

18. Governments usually possess the authority to obtain the information they require in the form of confidential reports made directly to them. For instance, corporations are required to submit information to government agencies overseeing such matters as taxation, security transactions, monopoly control, consumer protection, foreign exchange or price regulations.

19. In addition to the above, many Governments require the periodic submission of confidential special purpose reports needed for the preparation of surveys, the compilation of national accounts or balance of payments statistics, business trends and other statistical series. Some of these reports may be submitted on a voluntary basis by selected corporations. In the United States, for instance, reports are required for the preparation (at 5 to 10-year intervals) of surveys of foreign investment in the United States and United States investment in foreign countries; reports are also needed for the compilation of United States balance of payments statistics (monthly, quarterly and annual) and for surveys of domestic business activities. 6/ For some purposes, notably investigations into possible infringement of laws, such as tax evasion or monopolistic practices, Governments may seize or require the submission of corporate records and testimony by corporate executives.

20. The foregoing brief survey shows that, despite the vast amount of information contained in various reports of transnational corporations, much of it is not publicly available. The content of reports that are publicly available is fragmentary and lacks comparability. This reflects the absence of adequate disclosure requirements and accounting standards, especially at the international level.

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6/ See E/C.10/AC.1/3 for further information.

## II. THE NEED FOR INTERNATIONAL STANDARDIZATION

### A. The problem

21. The dual problem of inadequate information and lack of comparability of available information has been emphasized already. The type and amount of information which might be disclosed depends on the purpose and usefulness of the information and on an appreciation of the need for it in relation to the direct and indirect cost of providing it. In many countries, the emphasis has continued to be on the cost, influenced mainly by considerations of the confidentiality required to protect business and national interests. Moreover, it is often maintained that the information required to clarify specific issues, such as the nature and extent of possible monopolistic practices, artificial transfer pricing, social or environmental impact, may be so detailed as to render its inclusion in general purpose reports impracticable. On the other hand, the growing spread of the operations of transnational corporations and the rising interest in them and in their impact on society has heightened the demand for more information and has led to a reappraisal of disclosure requirements. A new balance is being sought concerning transnational corporations between freedom of information and protection of privacy.

22. The gaps in information and the lack of comparability with respect both to coverage and to the accounting standards used in their preparation are especially glaring in the case of many corporate annual reports. The contents of these reports vary as a result of varying national requirements for disclosure and the differing attitudes of corporations as regards voluntary disclosure. While the presentation of primary financial statements is generally required by law, corporations usually enjoy considerable latitude in respect of the level of disaggregation at which the financial information is presented. As far as non-financial information is concerned, disclosure requirements vary but are in general not extensive, so that the kind and amount of non-financial information included in these reports is largely determined by the reporting company itself.

23. The gaps in the information disclosed in these reports are many and various, but there are three particular areas in the consolidated financial statements of transnational corporations where disclosure is deficient, namely, geographical spread, line-of-business reporting and the reporting of intercompany transactions and balances. For instance, information on the geographical distribution of new investment and earnings is rarely presented. Further, there are various criteria for inclusion or exclusion of subsidiaries in the consolidated financial statements.

24. Variations in accounting practices are amply illustrated in a survey based mainly on 46 countries. 7/ For instance, in only 24 of the 46 countries surveyed are consolidated financial statements required or prepared by a majority of the companies, and in only 9 of the 46 countries is it a requirement or majority practice to carry investments in associated companies at equity rather than at cost. Even

7/ See E/C.10/AC.1/3.

more rare is an indication of the geographical spread of assets or earnings or similar information by industry lines. Individual companies in all but one of the major home countries of transnational corporations may use one or other of three different methods for the valuation of inventories. Most companies use the straight-line method of depreciation but some use an accelerated method. While the majority disregard the salvage value of the depreciated asset in computing depreciation, some companies deduct an estimated salvage value.

25. This lack of comparability because of the use of different accounting policies (principles and procedures) by various corporations is attributable to varying standards or to the lack of standards or clear guidelines at the national and international levels. In some countries the law prescribes the accounting principles to be observed with respect to certain items in the financial statements, but in general great latitude is left to the corporations. National accountancy bodies establish certain accounting standards to be observed by members of the profession, and these professional standards serve as guidelines for corporations in preparing their accounts, but their observance is usually not mandatory.

26. The extent and nature of differences in accounting and reporting practices in corporate reports are reviewed in document E/C.10/AC.1/3.

## B. Limited efforts for improvement

27. In spite of the clear need for improvement and standardization of reporting by transnational corporations, international efforts to this end have thus far been limited.

28. Some national efforts, however, are of particular relevance. In the United Kingdom, corporate accounting and reporting practices are currently under serious official study. A government consultative paper circulated by the Department of Trade in June 1976, entitled "Aims and Scope of Company Reports", states:

> "Few would dispute the view that companies have responsibilities to their employees and the community generally as well as to their shareholders and creditors and that these wider responsibilities may lead to a requirement to disclose further information."

29. The paper was issued to elicit the views of interested parties in connexion with an ongoing review of United Kingdom company law and its disclosure requirements. The document, which draws extensively upon The Corporate Report, a discussion paper commissioned by the Accounting Standards Steering Committee in 1974, 8/ suggests

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8/ "We have taken the view that financial reporting must cover a wider range of information than a narrow conventional interpretation of 'financial' /reporting/ would allow. We have endeavoured to propose the form and content of a package of information which will convey a rounded picture of economic activities rather than simply a view of financial positions and transactions." The Corporate Report, Accounting Standards Steering Committee, London, 1975, p. 10.

that among candidates for new statutory disclosure requirements the highest priority for further consideration should be given to: (a) a value-added statement; (b) an employment report; (c) a statement of future prospects; and (d) a statement of corporate objectives. Other proposed disclosures discussed in the paper cover source and use of funds statements, short-term debt, corporate pension funds, directors' interests, and efficiency indicators. Social accounting is also considered, but the paper observes that at present the law cannot play a significant role in this area. The Government considered that its task was to secure the uniform disclosure of the basic information needed to convey a rounded picture of corporate activities, while the accountancy profession would continue its efforts to achieve greater uniformity in the accounting standards and policies observed by corporations in the reporting of financial information.

30. In many other countries, efforts to improve corporate reporting have largely been a concern of the accountancy profession. In Canada, for instance, generally accepted accounting principles are established by the Canadian Institute of Chartered Accountants, which issues recommendations the observance of which is virtually mandatory under recent regulations to the Canada Business Corporations Act. In Australia, accounting standards are also set by the professional bodies, although some accounting principles are established by law. In the United States, the Government's approach to financial reporting is reflected in a 1973 statement of the Security and Exchange Commission that "... the Commission intends to continue its policy of looking to the private sector for leadership in establishing and improving accounting principles and standards through the Financial Accounting Standards Board (FASB)". 9/

31. At the regional level, the concern of Governments for the improvement and standardization of corporate reports has been evident in recent years. This is especially significant since the concern has been focused on transnational corporations. Thus, in the European Community, serious consideration has been given to disclosure and standardization requirements in connexion with the proposed European Company Law. The Guidelines for Multinational Enterprises of the Organization for Economic Co-operation and Development, endorsed by the Council of Ministers in June 1976, contains important provisions regarding disclosure of information. 10/

32. At the international level, efforts so far have mainly been limited to professional accounting organizations. The International Accounting Standards Committee, which was established in 1973, has issued several standards, including those for disclosure of accounting policies, valuation and presentation of inventories and consolidation. Approved standards on depreciation and information to be disclosed in financial statements are scheduled to be released in October 1976. Exposure drafts on other subjects have been circulated for comment by interested bodies. 11/

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9/ See E/C.10/AC.1/3.

10/ *Ibid.*

11/ *Ibid.*

33. The United Nations Group of Experts on International Standards of Accounting and Reporting is thus embarking on the first attempt of this kind at a global and multidisciplinary level. It is clear that the existing efforts and pronouncements on related matters by various public and private bodies merit serious consideration by the Group, and that duplication should be avoided. It is also clear that within a broad international framework the consideration of these matters necessarily involves a wide range of political, economic, social, cultural and legal implications of the operations of transnational corporations. The question of the standardization of accounting and reporting is thus not limited to financial spects or technical accounting issues, but involves the entire question of the requirement of information from transnational corporations by the world community.

## III. POSSIBLE INITIAL WORK

34. In embarking on this most important and complex task, the Group will have to decide on its objectives and on the ways in which these objectives may be achieved. As recognized by the Group of Eminent Persons, the establishment of a uniform international standard of accounting and reporting which would be followed by all transnational corporations is not feasible in the foreseeable future. Such an objective would require a degree of harmonization of national laws and regulations that has very little prospect of achievement, with the possible exception of some regional arrangements. An evolutionary approach is thus suggested. At the same time, even as a first step, the Group's objectives could go beyond general guidelines for greater disclosure and include specific recommendations on non-financial as well as financial items.

35. Also as envisaged by the Group of Eminent Persons, the initial work could concentrate on the formulation of an international standard which corporations could use in their annual reports as a basis for additional information. The Group might establish a minimum list which corporations could use on an experimental basis to supplement the information presented in their reports as a first step towards more comprehensive standardized reporting. The experience of corporations in using the minimum list would be useful for the formulation of a more comprehensive standardized accounting and reporting system.

### A. A possible minimum list

36. Possible items that might be included in a minimum list are presented in the annex that follows as an aid to discussion. The items are grouped under the following five broad headings:

A. Information to be disclosed in financial statements;

B. Accounting policies to be disclosed in the financial statements of transnational corporations;

C. Financial information on the members of transnational corporation groups;

D. Reporting on segments of a transnational corporation;

E. Non-financial information to be presented in annual reports.

The items under A, B, C and D pertain mainly to financial information, while those under E pertain primarily to non-financial information.

37. The balance sheet and income statement items in A are mainly those proposed by the International Accounting Standards Committee (IASC) in an exposure draft (IASC ED5) which was released for comment in June 1975. The list includes intercompany items that would not appear in a consolidated statement but should be disclosed in the statements of individual members of an enterprise group. The list of income statement items in IASC ED5 was expanded to include the data required for a rough estimate of the value added by the corporation. Some corporations already include full value-added statements in their reports and the United Kingdom Government is considering a proposal to require such an inclusion by law.

38. The last item, a source and use of funds statement, is the subject of an exposure draft (IASC ED7) issued with a view to the establishment of a separate international standard. Its inclusion in a minimum list is suggested because of the widespread interest in this information, which is reflected in the presentation of flow-of-funds statements in an increasing number of corporate reports. In a few countries it has recently been accorded the status of a primary financial statement, which corporations are required by law to publish along with the balance sheet and income statement.

39. The items in B, Disclosure of accounting policies, proposed for inclusion in the minimum list, are more specific than the international standards issued by the IASC (IAS 1, "Disclosure of accounting policies" and IAS 3, "Consolidation"). The uniform disclosure of the policies adopted, at least in those areas which are of particular importance in the reports of transnational corporations, is regarded as an essential feature of standardized accounting and reporting by such corporations.

40. The items in C, Financial information on the members of transnational corporation groups, relate to the disclosure of information on the structure of transnational corporations and the geographical distribution of their units and on selected intercompany transactions and balances. In the preparation of consolidated financial statements for a transnational corporation group, intercompany transactions and intercompany balances (i.e. intercompany loans outstanding and intercompany investment as of the balance-sheet data) are eliminated. The disclosure of this information in supplementary tables to the consolidated financial statements will make it possible to assess the degree of interdependence of the operations of the units of a transnational corporation group. Data on intercompany sales and lending during the reporting period will also shed light on the importance of the transnational corporation in world trade and international private lending and the role of transactions outside the regular market channels.

41. The items, in D, Reporting on segments of a transnational corporation, are directly addressed to transnational corporations. They are designed to show the geographical and industrial spread of these corporations. They should also aid in

the analysis of the performance and the contribution of units located in different economic environments, or engaged in different types of activities. This information also facilitates an appraisal of future prospects and risks.

42. The items in E illustrate the types of non-financial information to be reported. They are arranged by subject matter, under the headings Employment and Pollution control measures. Such information could be presented either in a separate section of the annual report or in a separate report; whichever approach is adopted, all the relevant information should be presented in one place, even if some items are also covered in the financial statements. In view of the special interest in information on various aspects of employment, wages and fringe benefits, in both home and host countries, and of the limited amount of information on these matters which is currently presented in most corporate reports, it might be suggested that corporations should publish data for some years preceding the year in which the first current employment report is presented.

## B. Possible procedure for establishing a minimum list

43. The Group might first decide whether the substantive discussion of a minimum list should be organized under the five suggested headings. The Group could then identify the items to be included under each heading of the list. Since the items in the suggested list are numerous, the Group might wish to establish working groups, each of which would consider a number of related items, recommend deletions or additions as required, elaborate on the definition for each item and, where appropriate, indicate whether the accounting principles should be uniformly specified or should be left to, and disclosed by, the corporations. Once a provisional list is established by the Group, it might be circulated for comment by corporations, labour groups, accountancy bodies, governments and other interested parties. These comments could be forwarded to the Centre on Transnational Corporations which would analyse them and prepare a report for the consideration of the Group, with a view to possible amendments.

## C. Possible further work

44. Concentration on the preparation of a minimum list necessarily emphasizes general purpose uniform reporting. This is perhaps the most basic objective when the purpose is multiple and the audience world-wide. It is by no means a substitute for much more detailed reporting for specific purposes and users. In particular, from the point of view of developing host countries, it might be useful to consider precisely what information should be required of transnational corporations operating in their territories and how such information may best be obtained. While information of this kind is likely to be detailed and to vary from case to case and country to country, and will frequently be confidential in nature, the Group might wish to consider at some stage a set of recommendations for this purpose. Some of the possible areas for consideration are briefly discussed in document E/C.10/AC.1/4.

## Annex

### A POSSIBLE MINIMUM LIST OF ITEMS TO BE REPORTED BY TRANSNATIONAL CORPORATIONS

### A. Main items in financial statements

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| BALANCE SHEET | | |
| Long-term assets | (EC4 - 8<br>(EC4 - 9 | |
| 1. Property, plant and equipment (gross) | IASC - ED 5 | (i) Translate foreign at historical or current exchange rate.<br>(ii) Carry at historical cost or at appraised values or at indexed amounts.<br>(iii) Re: own construction, carry at direct cost plus an appropriate portion of overhead or at direct costs only.<br>(iv) Include or exclude interest during construction.<br>(v) Retain in gross amount fully depreciated assets until physically retired or retire in year asset becomes fully depreciated.<br>(vi) An alternative is not to capitalize and depreciate hire purchase contracts, reporting only leasehold expense. |
| 2. Other long-term assets | IASC - ED 5 | |
| (a) Investments | | |
| (i) Subsidiaries consolidated[a/] | IASC - ED 5 | |
| (ii) Subsidiaries not consolidated | IASC - ED 5) | Carry at equity or at cost. |
| (iii) Associated companies | IASC - ED 5) | |
| (iv) Other investments | IASC - ED 5 | (i) Carry at market, or<br>(ii) At cost or market, whichever is lower, or<br>(iii) At cost, or<br>(iv) Cost less any permanent impairment. |
| (b) Long-term intercompany receivables[a/] )<br>(c) Other long-term receivables ) | IASC - ED 5 | Alternative is to discount long-term receivables having only nominal or no interest terms. |

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| (d) Purchased goodwill | IASC - ED 5 | (i) Mandatory, systematic amortization, or<br>(ii) Reduce only on basis of observed loss of value, or<br>(iii) Write off to surplus in year of acquisition. |
| (e) Patents, trademarks and similar | IASC - ED 5 | |
| (f) Deferred charges (describe) | IASC - ED 5 | |
| Current assets | (EC4 - 8<br>(EC4 - 9 | |
| 1. Cash on hand and in banks and short-term deposits | IASC - ED 5 | |
| 2. Marketable securities (other than investments) | IASC - ED 5 | (i) Carry at market, or<br>(ii) At cost or market, whichever is lower, or<br>(iii) At cost, or<br>(iv) Cost less any permanent impairment in value;<br>(v) If carried at cost market, value is or is not disclosed. |
| 3. Receivables<br>(a) Accounts and notes - Trade<br>(b) Directors and officers<br>(c) Intercompany a/<br>(d) Other | IASC - ED 5 | (i) Write off specific uncollectible accounts, or<br>(ii) Provide an allowance as a percentage of all doubtful accounts, or<br>(iii) Maintain a percentage of the receivable balance. |
| 4. Inventories | IASC - IAS 2 | (i) Carry at the lower of cost and net realizable value or at cost. (Some mining companies carry inventories at net realizable value.)<br>(ii) Include an appropriate portion of overhead in cost or carry only direct costs.<br>(iii) Determine the cost of items by the FIFO, average cost or LIFO method. If LIFO, disclose current cost or not.<br>(iv) Unsystematic (income levelling). |
| 5. Prepaid expenses (describe) | IASC - ED 5 | |

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| Long-term liabilities | (EC4 - 8<br>(EC4 - 9 | |
| 1. Loans (other than intercompany)<br>(indicate maturity dates and amounts))<br>)<br>2. Intercompany loans a/ ) | IASC - ED 5 | Alternative is to discount long-term debt having only nominal or no-interest terms. |
| 3. Pensions (private plans) | - | (i) Accrue an estimated pension for each individual employee for every hour worked, or<br>(ii) Accrue for vested rights only, or<br>(iii) Account on a "pay as you go" basis. |
| Current liabilities | (EC4 - 8<br>(EC4 - 9 | |
| 1. Bank loans and overdrafts | IASC - ED 5 | |
| 2. Current portions of long-term liabilities | IASC - ED 5 | |
| 3. Payables | IASC - ED 5 | |
| (a) Accounts and notes - Trade<br>(b) Directors and officers<br>(c) Intercompany a/<br>(d) Taxes on income<br>(e) Dividends<br>(f) Other accounts payable and accrued expenses | | |
| Other liabilities and provisions | (EC4 - 8<br>(EC4 - 9 | |
| 1. Deferred taxes | IASC - ED 5 | (i) Comprehensive or<br>- liability method<br>- deferred method<br>(ii) Partial, say five-year estimated turn-around, or<br>(iii) Pay as you go. |
| 2. Deferred income | IASC - ED 5 | Income not deferred even when<br>(i) Collection for sale is in doubt, or<br>(ii) Sale recorded notwithstanding substantial unperformed work or service. |
| 3. Provisions for warranties | IASC - ED 5 | |

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| 4. Potential losses on firm sales or purchase contracts | - | |
| 5. Other provisions (describe) | - | |
| <u>Shareholders' equity</u> | | |
| 1. Amount and description of each class of share capital and movements for the period. | IASC - ED 5 | |
| 2. Amount and movements for the period: (a) Capital paid-in in excess of par (b) Revaluation surplus (c) Reserves (d) Retained earnings | | Alternative is to use equity accounts to transfer income between periods, often to absorb charges which would otherwise be against income of current or future years. |
| <u>Balance sheet foot-notes</u> | | |
| 1. Restrictions on (a) Cash (b) Title to assets or liens | IASC - ED 5 | |
| 2. Lease commitments quantified (describe leasehold) | - | |
| 3. Contingent assets and liabilities (quantified if possible) | IASC - ED 5 | |
| 4. Contracts for future capital expenditure (omit small amounts which can be met with current working capital) | IASC - ED 5 | |
| 5. Material events that have occurred after the balance sheet date (quantified if possible) | IASC - ED 5 | |
| 6. Pensions earned but not provided for | - | |
| INCOME STATEMENT | (EC4 - 20 (EC4 - 21 | |
| <u>Revenue</u> | | |
| 1. Sales or other operating revenue | IASC - ED 5 | See comments under "Deferred income" above. |

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| 2. Interest and investment income | IASC - ED 5 | |
| 3. Equity in income of associated companies | - | Alternative is to carry such investment at cost and report as income only dividends received (see comments under "Associated companies" in the balance sheet). |
| **Costs and expenses** | | |
| 1. Cost of goods sold | - | See comments under "Inventories". |
| 2. Other operating expenses | - | |
| 3. Selling, general and administrative expenses | - | |
| 4. Depreciation | IASC - ED 5<br>IASC - ED 4 | ( (i) Straight-line over useful life;<br>( (ii) Accelerated;<br>((iii) Unit of production;<br>( (iv) Unsystematic (income leveling). |
| 5. Interest expense | IASC - ED 5 | |
| 6. Significant intercompany transactions[a] | IASC - ED 5 | Intercompany revenue, costs and expenses may be reported in other captions and may or may not be qualified in the foot-notes. |
| 7. Taxes on income | IASC - ED 5 | See comments under "Deferred taxes" above. |
| 8. Unusual charges and credits | IASC - ED 5 | Alternative is to enter such charges directly into shareholders equity accounts. |
| **Net income** | IASC - ED 5 | An alternative reporting practice is to omit certain costs and expenses from income statement while the same amount of net income is reported. |

Income statement foot-notes

1. Classify the total of:

   Cost of goods sold, other operating expenses, selling, general and administrative expenses as:

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| (a) Materials and services purchased | - | |
| (b) Wages and salaries paid | - | |
| Disclose: | | |
| 2. Research and development | OECD - GL | |
| Amount capitalized and amount expensed directly during the period | | |
| 3. Pension expense | | |
| See comments under "Pensions" in the balance sheet | | |
| 4. Leasehold expense and commitment | | |
| See comments under "Property, plant and equipment" | | |
| 5. See comments under "Significant intercompany transactions" above, e.g. disclose significant intercompany dividends, sales, purchases, interest, royalties, licence fees, rentals for use of tangible property, research and development, management services and other allocated expenses. | | |
| STATEMENT OF SOURCES AND USES OF FUNDS | IASC - ED 7<br>OECD - GL | |
| A statement of sources and uses of funds may account for either the change between periods in working capital or cash and temporary cash investments, provided the change reported is determinable from the face of the balance sheet. | | |
| The statement may begin with net income shown in the income statement and add and deduct items not requiring working capital or cash. Or the statement may omit non-cash items by beginning with revenue and arriving at the working capital provided by operations. | | |
| In addition to showing working capital or cash provided from operations the statement should disclose all other financing and investing activities for the year, such as: | IASC - ED 7 | |

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| (a) Proceeds from sale of long-term assets | | |
| (b) Outlays for purchase of long-term assets | | |
| (c) Cash dividends and non-cash dividends, including dividends by subsidiaries to minority interests | | |
| (d) Issue, redemption, and repayment of long-term debt, reclassification of short-term portion of long-term debt, and conversion of long-term debt to common or ordinary shares | | |
| (e) Issue of shares for cash or other assets and redemption or purchase of shares for cash or other assets | | |
| (f) Conversion of preferred shares to common or ordinary shares | | |
| As a subtotal it is desirable that the statement show the funds provided from or used in operations. | | |

## B. Disclosure of accounting policies

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| The notes to the financial statements should disclose all significant accounting policies which have been used, including over-all valuation policies (e.g. historical cost, general purchasing power, replacement value). | (IASC - IAS 1<br>(OECD - GL | |
| A transnational corporation should describe at length its policies relative to intercompany transactions and segmentation of consolidated information, for example: | | |
| 1. Consolidation policy: | ( EC7<br>(IASC - IAS 1<br>(OECD - GL | |
| (a) Basis for inclusion and exclusion of subsidiaries in consolidation | IASC - IAS 3 | |
| (b) Basis for carrying associated companies | IASC - IAS 3 | |
| (c) Basis for elimination of intercompany profits | - | |
| (d) Method of translating foreign accounts | IASC - IAS 1 | |
| 2. Method of determining transfer prices of products or parts | OECD - GL | |

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| 3. Basis for determining intercompany charges for:<br>(a) Interest<br>(b) Royalties<br>(c) Licence fees<br>(d) Rental for use of tangible property<br>(e) Other intangibles | - | |
| 4. Method of allocating expenses among members for:<br>(a) Research and development<br>(b) Advertising<br>(c) Management services<br>(d) Other allocated expenses | - | |
| 5. Basis for the selection of geographical areas reported separately | - | |
| 6. Basis for segmentation by industries or types of products or services reported separately | - | |

C. Financial information on members of a transnational corporation group

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| 1. List of significant subsidiaries and percentage ownership (by geographical area of operation), justify exclusion of any such subsidiaries from consolidation. Carry excluded subsidiaries at equity or disclose equity in the foot-notes. | (IASC - IAS 3<br>(OECD - GL | |
| 2. List of associated companies and nature of relationship with parent company (by geographical area of operation). Justify carrying such investments at other than equity and disclose equity in the foot-notes. | (IASC - IAS 3<br>(OECD - GL | |
| 3. Disclosure of identity of parent company in reports of subsidiaries. | | |
| 4. Disclosure of information on the following (eliminated in consolidated statements)<br>(a) Intercompany sales<br>(b) Intercompany charges for interest, royalties, licence fees, rental for use of tangible property and other intangibles | | |

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| (c) Intercompany charges for research and development, advertising, management services and other allocated expenses | | |
| (d) Net increase (decrease) in intercompany investments | | |
| (e) Net increase (decrease) in intercompany loans | | |

## D. Reporting on segments of a transnational corporation

### Segmentation by geographical areas

| | | |
|---|---|---|
| 1. Assets or net assets | IASC - IAS 3 | (i) Report segment assets according to the risk of operating in foreign countries; the location of the subsidiary is not taken without analysis and reclassification of its assets, such as bank accounts, accounts receivable inventory at still another geographical area, or<br>(ii) Report on the basis of the books of the subsidiary without regard to reclassification, on the basis that the books hold appropriate assets for the measurement of return on investment. Note: net assets are often not disclosed because of the difficulty of tracing borrowed funds to countries where they are employed. |
| 2. Revenue | (IASC - IAS 3<br>(OECD - GL | (i) Attribute revenue to the geographical area of the last significant value added, or<br>(ii) Classify revenue according to the geographical area of the customer (see also under 3 below). |
| 3. Earnings (results of operations) | OECD - GL | (i) Attribute revenue to the geographical area of the last significant value added (a general interest concept - transfers at cost), or<br>(ii) Employ transfer pricing showing revenue separately as to sales to unaffiliated customers and interregional sales within the corporation. |

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| 4. As to each balance sheet and income statement caption, disclose any exposure to exceptional risks | IASC - IAS 3 | |
| 5. Describe principal activities in each area | OECD - GL | |
| 6. New capital investment | OECD - GL | |
| <u>Segmentation by industries</u> | | |
| 1. Identifiable assets by industries | | |
| 2. Disclose other assets to reconcile to total assets shown in the balance sheet | | |
| 3. Revenue by industries and show intersegment sales separately | OECD - GL | |
| 4. One or more of (by industries)<br>(a) Profit contribution<br>(b) Operating profit<br>(c) Profit before taxes<br>(d) Net profit | | |
| 5. New capital investment | OECD - GL | |

## E. Some items in non-financial reporting

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| 1. Employment report (total and by geographical areas reported) | | |
| (a) Number employed at year end | OECD - GL[b/] | |
| (b) Number of expatriates employed at year end | | |
| (c) Number of women employed at year end | | |
| (For (a), (b) and (c) above also report, if possible, change in number employed during year) | | |
| (d) Number employed at year end by function:<br>Production<br>Other | | |

| | Relevant international pronouncements | Some alternative accounting principles |
|---|---|---|
| (e) Average hours worked per week per employee | | |
| (f) Employee costs | | |
| (i) Total wages and salaries | | |
| (ii) Total cost of fringe benefits (list benefits) | | |
| (iii) Cost of training schemes | | |
| (g) Description of pension plan | | |
| 2. Report on pollution-control measures | | |
| (a) Capital and other non-recurrent costs | | |
| (b) Current expenses | | |
| (c) Description of achievements | | |

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a/ Not applicable to consolidated financial statements.

b/ OECD guidelines call for average number employed during reporting period.

Key:

| | |
|---|---|
| IASC - ED (number) | International Accounting Standards Committee, Exposure Drafts |
| IASC - IAS (number) | International Accounting Standards Committee<br>International Accounting Standards |
| OECD - GL | Organization for Economic Co-operation and Development, Guidelines for Multinational Enterprises |
| EC 4 (number) | Commission of the European Communities, Proposal for a Fourth Council Directive (numbers refer to articles) |
| EC 7 | Commission of the European Communities, Proposal for a Seventh Council Directive |

## 2. INTERNATIONAL STANDARDS OF ACCOUNTING AND REPORTING*

### INTRODUCTION

1. Traditionally corporate annual reports are primarily oriented to the information needs of the corporation's shareholders and creditors. The original purpose of the laws requiring annual public reporting by corporate entities was explicitly to enable shareholders and creditors to appraise the conduct of the corporation's affairs. As corporations have grown and their importance has extended beyond national boundaries, their activities have attracted the keen interest of a widening circle of individuals and groups not confined to the original users of corporate reports. To meet some of the information needs of these groups, Governments of several countries have broadened reporting requirements to provide for additional information. A number of national accountancy bodies, for their part, have intensified their efforts to formulate and gain general acceptance for certain basic accounting and reporting standards. In addition, some transnational corporations, recognizing the importance of greater openness in the reporting of their activities, have voluntarily enlarged the scope of their annual reports.

2. Despite these efforts, however, corporate reports continue to vary considerably with respect to the quantity of information disclosed and the accounting policies and practices observed in their preparation. Differences in the reports of corporations established in different countries are particularly marked, but the content and presentation of reports issued in the same country also vary significantly.

3. Noting the need for improved corporate reporting, the Group of Eminent Persons appointed to study the impact of these corporations advocated the formulation of an international, comparable system of standardized accounting and reporting. 1/ In order to prepare for such a system, the reasons for the existing diversity of practices need to be carefully examined. While differences in national laws and generally accepted accounting standards are important factors, diversity also results from the fact that corporations need to use various accounting policies in order to convey a "true and fair" picture of their financial position and performance. A standardized system does not therefore necessarily imply rigid uniformity in all accounting policies for corporations in differing and changing circumstances.

4. The approach of the International Accounting Standards Committee (IASC), to the formulation of standards indeed focused on the essentials so that the standards adopted would not be so complex as to be inapplicable on a world-wide scale. 2/ The Committee emphasized, furthermore, that the international accounting standards promulgated by it were not intended to override local regulations or

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* Originally issued as document E/C.10/AC.1/3, dated 30 July 1976.

1/ The Impact of Multinational Corporations on Development and on International Relations (United Nations publication, Sales No. E.74.II.A.5), p. 95.

2/ IASC, The Work and Purpose of the International Accounting Standards Committee, London, 1975.

accepted accounting standards. It recommended, however, that where national standards and practices differed significantly from the Committee's international standards, the fact should be disclosed in financial statements and auditors' reports and, if possible, a reconciliation of differences in results should be presented. The Group of Eminent Persons in the report referred to earlier 3/ also envisaged that the proposed international standard would coexist with rather than replace existing national standards in the foreseeable future, but that it would call for additional data to be included in the reports of transnational corporations.

5. The present paper is designed mainly to provide background information relative to the topics to be discussed by the Group of Experts on International Standards of Accounting and Reporting. Section I describes current practices in the issuance of general purpose financial statements and evaluates these practices on the basis of the accounting principles and reporting practices of companies in 46 countries. The survey is presented in tabular form in annex I. Section I also refers to numerous special purpose reports, some of which are illustrated in annexes II to IV. Ongoing efforts to achieve standardization of or better disclosure in general purpose financial statements at the national, regional and international levels are described in section II and annexes V to IX. These surveys inevitably concentrate on general purpose financial statements and little mention is made of non-financial items, which have been largely neglected, both in existing corporate reports and in efforts for their improvement.

3/ The Impact of Multinational Corporations on Development and on International Relations, op. cit., p. 95.

## I. ACCOUNTING AND REPORTING PRACTICES

### A. General purpose financial statements

6. The accounting principles and reporting practices applied in the preparation of general purpose financial statements have developed over the years in response to national environments, and there are now significant differences between countries and companies with respect to the principles and practices observed. These differences are clearly shown in a survey of the practices of companies in 46 countries. 4/ It should be noted, however, that the survey covers all corporations, not only transnationals, and the differences it reveals may be somewhat exaggerated for the latter. The survey is presented in annex I in condensed form and with the items regrouped, so as to be appropriate for a review of current practices relative to a transnational corporation. In the following pages some comments are presented on certain of the practices surveyed. These comments are based both on the survey and on experience in scrutinizing reports of transnational corporations.

#### 1. Consolidation

7. Principles and practices with respect to consolidation and the presentation of consolidated financial statements vary widely, as shown in table 1. In 9 of the 13 developed countries where most transnational corporations are domiciled, the presentation of consolidated statements is either mandatory or the practice of the majority of companies. In the other countries, only a relatively few companies prepare consolidated statements.

8. There are no generally accepted criteria for determining which subsidiaries are to be included in consolidated statements. 5/ While wholly-owned domestic subsidiaries are generally included, practices vary with respect to the inclusion of foreign wholly-owned and majority-owned subsidiaries. In a few countries the consolidation of majority-owned subsidiaries is mandatory, in some others it is either not permitted or not done by most companies. Minority-owned companies are generally not included in consolidated statements, even if the parent company has effective control.

9. In most countries where companies prepare consolidated statements, the presentation of these consolidated statements to parent company shareholders must be accompanied by parent company financial statements. This is not the case in the United States and Canada where most companies now prepare only consolidated statements.

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4/ A Survey in 46 Countries: Accounting Principles and Reporting Practices, Price Waterhouse International, 1975.

5/ Criteria have, however, been set forth in the recently released IASC: IAS 3, effective 1 January 1977.

**Table 1. Selected developed countries: Policies and practices relating to consolidation**

| Country | Conditions for inclusion in consolidated reports | | | Presentation of consolidated statements | | Investment in unconsolidated subsidiaries and associated companies: carrying basis | | Translation of foreign currency financial statements | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | With limited exceptions all domestic and foreign subsidiaries are consolidated | Ownership of 50 per cent or more is a prerequisite for consolidation | Less than 50 per cent owned companies included if investor has effective control | Consolidated statement only is prepared for shareholders | Consolidated statement accompanies parent company statement | Equity basis | Cost basis | Closing rate for monetary assets/liabilities and historic rate for non-monetary assets | Closing rate for current assets/liabilities historic rate for non-current assets/liabilities | Closing rate for all assets/liabilities |
| Australia....... | MA | R | R | NP | R | MI | MA | MA | MI | MI |
| Belgium......... | N | N | N | NP | N | N | N | N | N | N |
| Canada.......... | R | R | N | MA | MI | R | NP | MI | MA | MI |
| France.......... | H | MA | N | NP | H | MI | MI | MI | N | MA |
| Germany, Fed. Republic of .. | MI | NP | N | NP | R | NP | N | MI | MI | H |
| Italy........... | MI | MI | N | NP | MI | MI | MI | MI | MI | MI |
| Japan........... | R | R | NP | NP | MI | MI | MI | MI | MI | MA |
| Netherlands..... | MA | MA | N | NP | MA | H | MI | MI | MI | MA |
| Norway.......... | MA | MI | N | N | H | N | MA | N | N | MA |
| Sweden.......... | MA | MI | N | MI | H | N | MA | MI | H | H |
| Switzerland..... | MA | MA | N | NP | H | NP | MI | MI | MI | MA |
| United Kingdom.. | R | NP | NP | NP | R | MI | MI | MI | MI | MA |
| United States... | MA | R | NP | MA | N | R | NP | MA | MI | NP |

Source: Centre on Transnational Corporations, based on A Survey in 46 Countries: Accounting Principles and Reporting Practices, Price Waterhouse International, 1975.

Key:
- R Required by law or otherwise mandatory
- MA Practice of majority of companies
- H Practice of about half of companies
- MI Practice of minority of companies
- N Not found in practice or not applicable
- NP Not permitted

2. Equity accounting

10. Subsidiaries which do not qualify for consolidation, and associated companies (i.e. companies which are 20 to under 50 per cent-owned), are included in consolidated statements either at cost (that is at the original amount invested regardless of any subsequent reinvestment of earnings, with only dividends being reported) or by the equity method. Under the latter, the equity in the subsidiary company's financial position is reported in the consolidated balance-sheet and equity in net income is reported in the consolidated income statement. The equity method reflects more fully the contribution of unconsolidated subsidiaries and associated companies to the enterprise group as a whole. Except in several developed countries, where equity accounting is now mandatory, few companies use the equity basis and there is no uniformity in the practice of companies established in the same country. 5/

3. Foreign currency translation

11. For the purpose of preparing consolidated statements, the financial statements of foreign subsidiaries expressed in terms of the various host countries' currencies need to be translated into the currency of the parent company. At a time when exchange rates are subject to substantial fluctuations, the method of translation can significantly affect the results. The simplest method, which is still widely used by companies in western Europe, is the application of the closing rate to all items in the subsidiaries' financial statements. More sophisticated methods involve the use of different rates for the translation of different items. The majority of companies in the United States, for instance, distinguish between non-monetary assets, and monetary assets and liabilities, and apply the closing rate to the latter and the rate prevailing at the time of acquisition to the former. An alternative method, which is used by a majority of companies in Canada, is to apply the closing rate to current assets and liabilities and the historic rate to long-term assets and liabilities.

4. Inflation accounting

12. In an inflationary period, the basic accounting principle of recording all assets, liabilities and transactions at historical cost distorts the relationship between various items in the financial statements to a varying degree depending upon the prevailing rates of inflation. In the case of transnational corporations, such distortions are often very significant because of differing rates of inflation in the host countries of foreign subsidiaries. Most companies retain historical cost data in their primary financial statements, but a few supplement the basic statements with statements showing data adjusted for changes in the general price level or giving information on the replacement cost of assets.

13. There is no generally accepted practice with respect to accounting for the effects of inflation. In this connexion, the recently issued regulation of the United States Securities and Exchange Commission requiring corporations to present supplementary information on the replacement cost of inventories, property and

plant and equipment is noteworthy. Current purchasing power adjustments are found in many of the government statistics issued, but rarely in corporate reports.

5. Inventory carrying basis

14. Price fluctuations and inflationary price increases affect the value of goods in inventories. As shown in table 2 below, all or a majority of the companies in the countries surveyed carry inventories at the lower of cost or market price. Carrying inventories at either cost or market price alone is in most cases not permitted. Methods used for determining cost vary from company to company. The majority of companies use either the first-in-first-out (FIFO) or the weighted average method, but the last-in-first-out (LIFO) method is also used in a few cases. Surprisingly few countries require the disclosure of the carrying basis for inventories. In view of the variety of practices in this area, disclosure is in fact required under the first and second international accounting standards issued by IASC.

Table 2. Inventory carrying bases: selected developed countries

| Country | Cost | Market | Lower of cost or market | Cost determined by FIFO | LIFO | Weighted average method | Carrying basis disclosed | Undisclosed under-valuation of inventories practised |
|---|---|---|---|---|---|---|---|---|
| Australia ........ | N | N | MA | MA | N | MI | MI | N |
| Belgium........... | MI | N | MA | MA | MI | MI | MI | NP |
| Canada............ | NP | NP | R | H | MI | H | MI | NP |
| France ........... | MI | NP | MA | H | NP | H | MI | NP |
| Germany, Fed. Republic of..... | NP | NP | R | MI | MI | H | R | NP |
| Italy............. | NP | NP | R | MI | MA | MI | MI | MA |
| Japan............. | NP | NP | MA | MI | MI | MA | R | NP |
| Netherlands....... | NP | MI | MA | MA | MI | MI | H | NP |
| Norway............ | NP | NP | R | H | NP | H | MI | H |
| Sweden............ | NP | N | MA | MA | MI | MI | MI | H |
| Switzerland....... | NP | NP | MI | H | MI | MI | MI | MA |
| United Kingdom.... | NP | NP | R | R | NP | NP | R | NP |
| United States..... | NP | NP | R | MA | MI | MI | R | MI |

Source: Centre on Transnational Corporations, based on A Survey in 46 Countries: Accounting Principles and Reporting Practices, Price Waterhouse International, 1975.

Key:
- R Required by law or otherwise mandatory
- MA Practice of majority of companies surveyed
- H Practice of about half of companies surveyed
- MI Practice of minority of companies surveyed
- N Not found in practice or not applicable
- NP Not permitted
- FIFO First-in-first-out
- LIFO Last-in-first-out

## 6. Income levelling

15. A large number of companies in some developed countries use reserves to level income reported by periods. While prudence is considered a virtue, there can be no short-run comparison of the results of companies in the United States, for example, where contingencies are not provided for and contingency reserves are not available to draw from, with companies in many developed countries in Europe, where income is levelled, often for tax purposes as well.

## 7. Geographical spread

16. Information on the geographical spread of assets, by areas, and on the geographical source of income is rarely adequate. Geographical information on source of sales is somewhat more frequently found. The adequacy of standards of disclosure in this connexion is dependent on standards of accounting principles relative to: (a) transfer pricing and royalties; (b) allocation of home country research and development and headquarters services and expenses; and (c) an allocation of income taxes relative to such items reclassified for financial statement purposes but not similarly treated for tax purposes. It should be noted that many would not allocate interest, general and administrative expenses or income taxes.

## 8. Line of business

17. Information on lines of business is rarely adequate. Sales by line of business is somewhat more frequently found. The adequacy of standards in this connexion is dependent on matters described above under geographical spread. In addition, criteria for the definition of a line of business is needed.

## 9. Other matters

18. As shown in annex I, many other matters are not treated uniformly. Although different accounting standards reduce the comparability of transnational corporation reports, the consistent use of certain standards together with the disclosure of the corporation's accounting policy facilitates comparisons to some extent. On the other hand, if certain items of information are not disclosed - though included in the main aggregates - there is no way of filling the gap.

## B. Translations and adjustments for transnational users

19. Some transnational corporations, recognizing the differing requirements of transnational users of general purpose financial statements, have adopted various practices to improve the understanding of their reports.

20. A most obvious aid for the convenience of the user is to translate the statements into the language familiar to him. Another aid is to translate the statements into the currency of the user. A further aid is to present financial

statements in accordance with the local accounting standards. There are a variety of ways in which these translations or adjustments are presented.

21. In addition to the primary (country of domicile) statement, a few transnational corporations issue secondary general purpose financial statements (usually for users of another country) with the appropriate translations of language and currencies and adjustments of standards. Procedures of this kind are costly and usually undertaken in only one or two foreign languages.

22. Some transnational corporations issue dual purpose (primary) financial statements. These are more frequently found in the English language. The primary financial statements in English may be expressed in, say, pounds, the currency of the company's country of domicile, while in the foot-notes or a prominent schedule attached there is a reconciliation of net income, in accordance, say, with United Kingdom standards and United States standards. Usually only some five or six reconciling items appear, all of which are shown in both pounds and dollars. This procedure is frequently used where the differences are few.

23. Another variant is to present additional columns for the convenience of the user. Adjacent to the primary financial statements, there are columns in a foreign currency translated at the closing rate of exchange. Often a foot-note is attached to this type of statement, which may read, for example:

> "This translation should not be construed as representing that United States dollar [currency of country of domicile] amounts actually represent, or have been or could be converted into, Deutsche Marks [currency into which statement is translated]."

24. The general purpose financial statements of a foreign subsidiary issued in the host country may be in accordance with local standards and expressed in the currency of the host country. These statements are adjusted to the accounting principles of the parent, translated into the currency of the home country and combined with the statements of other subsidiaries, both foreign and domestic, in the process of preparing consolidated financial statements.

25. It has been proposed that if international accounting standards are established and accepted, an added column should be included in financial statements in order to present financial information in accordance with these standards. This could be combined with primary financial statements presenting the information in accordance with the accounting and reporting standards of the country of domicile and secondary statements presenting the information in accordance with the standards of a second country, both expressed in the currencies of the country of domicile and the second country. Column headings of such comparative financial statements might be as follows:

| Primary | | | | Secondary | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Accounting principles generally accepted in the United States | | | | True and fair view in the United Kingdom | | | | International standards | | | |
| 1975 | | 1976 | | 1975 | | 1976 | | 1975 | | 1976 | |
| $ | £ | $ | £ | $ | £ | $ | £ | $ | £ | $ | £ |

## C. Special purpose reports

26. The types and uses of special purpose reports have been discussed in document E/C.10/AC.1/2. Briefly, these reports submitted directly to Governments are usually kept confidential. Since they are designed to satisfy the information needs of the governmental agency to which they are submitted, their form and content vary from country to country. The requesting agency sets the reporting standard for all the corporations concerned. The kinds of information collected by Governments were described in document E/C.10/11/Add.1 submitted to the second session of the Commission on Transnational Corporations. The scope and nature of the information which corporations have to make available on a regular basis is illustrated by the reports to the United States Government described in annexes II to IV, together with summaries of the main reporting forms.

## II. EFFORTS TO ACHIEVE STANDARDIZATION

27. Efforts to achieve standardization of accounting principles and methods are being undertaken at the national, regional and international levels. Unless there is some degree of co-ordination of the activities at different levels, there is a risk that standardization at the national level might solidify positions in each country and make standardization or harmonization within a regional or international framework more difficult.

### A. National efforts

28. Differences in the accounting and reporting practices applied by corporations domiciled in the same country result in part from the traditional reliance of Governments on the accounting profession for the regulation of financial accounting. Laws usually prescribe the basic form and general content of the financial statements of public corporations, but they rarely specify the standards to be observed in their preparation. The main responsibility for establishing standards is undertaken by national accountancy bodies or special boards, such as the Financial Accounting Standards Board in the United States. These bodies issue pronouncements which may be mandatory in the sense that members of the profession are required to see that the pronouncements are adhered to or to disclose departures in connexion with the examination of financial statements. Alternately, they may be issued in the form of guidelines for professional accountants. As a rule, standards are established one by one, rather than as part of a comprehensive system, and do not deal with all aspects of financial accounting and reporting. Consequently, companies usually enjoy a large degree of freedom with respect to the choice of accounting policies to be used in preparing financial statements.

29. In recent years, efforts to establish standards have been intensified in several countries. In the United States, for instance, at the end of 1975 financial reporting was governed by 51 accounting research bulletins, 31 Accounting Principles Board opinions, together with several hundred related interpretations, 12 Financial Accounting Standards Board (FASB) statements, and 187 accounting series releases of the Securities and Exchange Commission. The FASB, established in 1973, now has responsibility for establishing financial accounting standards. The steps leading to the issuance of a standard include the preparation and distribution of a discussion memorandum, followed by a public hearing and the preparation of an exposure draft which is issued for public comment. These comments are taken into account in preparing a final draft. A statement of financial accounting standards is then issued. The standards-setting organizations in several other developed countries (e.g. Australia, Canada, the United Kingdom) now follow a similar pattern of issuing proposed standards (in exposure drafts) for comment by interested persons. Responses are then evaluated and final standards issued for members of the leading professional organizations.

30. In Canada, where each of the 10 provinces has a professional organization, the Canadian Institute of Chartered Accountants (CICA) is the national co-ordinator

for promoting uniformity of standards among the provincial institutes. Since 1975, the recommendations of CICA have effectively been given the status of statutory requirements. In Australia and the United Kingdom, the practice of establishing accounting standards which are binding on members of the accounting profession is of recent date. Until the early 1970s, the national accountancy bodies confined themselves to the issuance of recommendations and guidelines, the application of which was not mandatory.

## B. Regional efforts

31. There are several regional multinational accounting organizations which meet periodically to discuss problems common to their membership. One such group, the Accountants International Study Group (AISG), publishes studies comparing practices in Canada, the United Kingdom and the United States. Other regional organizations are the Confederation of Asian and Pacific Accountants (CAPA), the Inter-American Accounting Association (IAA) (representing members from the western hemisphere), and the Union Européenne des Experts Comptables Economiques et Financiers (UEC).

32. A serious attempt at harmonizing accounting practices is being made in the European Communities (EC). Common market membership carries with it a commitment to harmonize local laws in accordance with decisions of the EC governing bodies. The Commission of the European Communities has submitted to the Council of the European Communities several proposed directives and has for several years been working within the membership to develop standards that will be acceptable to the member countries.

33. The proposed Fourth Directive would standardize the annual accounts of limited companies. It encompasses the accounts, disclosure standards, and the form and scope of the auditor's report. The proposed Seventh Directive deals with the concept and mechanics of consolidations, a subject which deserves early, separate attention. So far these directives have not been issued by the Council and are not binding on member countries.

34. Guidelines for Multinational Enterprises, issued by the Organization for Economic Co-operation and Development (OECD), contains a section on Disclosure of information. The entire text of this section is reproduced in annex V.

35. The formation of more so-called economic communities is bound to result in an increase in the number of regional accounting organizations, or an increase in the extent to which accountants in such regions work together within a broader organization.

## C. International efforts

36. Current efforts to formulate and promote the adoption of a set of basic international standards to be observed in the presentation of audited accounts and financial statements could make an important contribution towards improved

financial reporting by transnational corporations. If these efforts were to succeed in establishing an international accounting framework, the comparability of corporate financial statements would be greatly enhanced. Efforts of this kind are being undertaken by IASC, established in 1973 by the major accountancy bodies of nine countries. A list of the members and associate members as of July 1976 is shown in annex VI.

37. The objectives of the IASC are to formulate and publish, in the public interest, basic standards to be observed in the presentation of audited accounts and financial statements, and to promote their world-wide acceptance and observance. In formulating these standards the Committee takes into account existing national standards, in order to achieve a substantial degree of compatibility between the standards it issues and those already in use.

38. The IASC decided that in order to facilitate the application of the international standards, it would confine them to essentials. The Committee's agenda in September 1975 provided for the formulation of 13 international standards in the years 1974 to 1977 (see annex VI). To date, seven standards have been formulated, five of which have already been approved and issued. Exposure drafts for the other two have been issued for comment. It is noteworthy that some matters of particular importance to reporting by transnational corporations, notably the geographical breakdown of consolidated information, is not included in the present IASC agenda.

39. The degree of authority which attaches to the promulgation of international accounting standards is limited. The accounting profession cannot enforce its decisions except on its own members. To gain acceptance for the standards, it has to proceed by persuasion and example. It can impose sanctions, however, on those of its members who fail to ensure that accounts comply with these standards or that departures from them are disclosed.

40. IASC standardization efforts focus on corporate accounting and financial reporting and do not address themselves to other aspects of corporate reporting. Nor do they deal specifically with special purpose reporting of financial information, chiefly of interest to particular users of transnational corporation reports. Hence, even if IASC efforts achieve all their present objectives, many of the issues raised by the reporting practices of transnational corporations will not have been dealt with.

41. One of the proposals made which could lead to intensified efforts to establish world accounting standards and to a greater degree of acceptance by the profession is the formation of an International Federation of Accountants (IFAC) and a permanent secretariat. The proposed objectives of IFAC are to establish uniform world standards for auditing, professional ethics, and professional education and training. This proposal will be considered by some 100 professional accounting bodies from 71 countries at the Eleventh International Congress of Accountants to be held in October 1977.

42. The Group of Experts on International Standards of Accounting and Reporting

will undoubtedly wish to take account of existing practices and efforts in its work. At the same time, it is also clear that the Group will have to consider a broad range of issues not so far adequately dealt with elsewhere. Thus, it will be concerned not only with shareholders and creditors but with the public interest in general. It will not be confined to the task of setting accounting standards but will also seek to clarify what is to be disclosed. It will not restrict its field to the improvement of financial statements but will also concern itself with non-financial reporting. These difficult and complex tasks will demand not only drawing upon existing efforts but the breaking of new ground.

## Annex I

SURVEY OF ACCOUNTING AND REPORTING STANDARDS a/

The Survey shows, for selected standards, the existing (1974) corporate reporting practices in 46 countries and the current efforts by the International Accounting Standards Committee and the Organisation for Economic Co-operation and Development in the formulation of international standards.

Contents



a/ Centre on Transnational Corporations, based on A Survey in 46 Countries: Accounting Principles and Reporting Practices, Price Waterhouse International, 1975.

## Key to tables

### Column 1

The first number for each entry under Practice Survey corresponds to the number of the principle or practice in A Survey in 46 Countries: Accounting Principles and Reporting Practices. Below this, the first set of coupled numbers indicates first the number of countries where the practice is required or is applied by the majority of issuers of financial statements and second the number of countries surveyed.

The second set of coupled numbers gives the same information for the 19 developed countries included in the Survey in 46 Countries. The Survey reflects practices in 1974.

### Column 2

IASC: International Accounting Standards Committee

IAS (number): international accounting standard issued by IASC

ED (number): exposure draft of IASC. The number or numbers shown below IAS and ED indicate the paragraphs of the IAS or ED referred to.

### Column 3

OECD-GL: Organization for Economic Co-operation and Development: Guidelines for Multinational Enterprises. The number shown in the column refers to the relevant item listed in OECD-GL under the heading "Disclosure of information".

## I. BASIC STANDARDS

### A. Objectives of financial statements a/

1. Description of objectives.
2. Definitions of:
   (a) Assets to be included in financial statements;
   (b) Contingent assets to be disclosed in foot-notes;
   (c) Expenses of the period;
   (d) Liabilities to be included in financial statements;
   (e) Contingent liabilities to be disclosed in foot-notes;
   (f) Revenues earned in the period.

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a/ No authoritative pronouncement has been made by any national organization of professional accountants although several have been actively studying the matter. Many accountants believe that the general acceptance of a description of the objectives of financial statements will have a considerable effect on a few fundamental concepts, and little effect on most of the more numerous accounting principles and reporting practices. Most accountants agree that the absence of an accepted description of objectives is a void that should be filled as soon as possible.

## B. Fundamental accounting concepts

| | Practice survey | IASC | OECD-GL |
|---|---|---|---|
| 1. Departures from the following fundamental accounting assumptions are disclosed: | No. 7 | IAS 1 | |
| (a) Going concern | 38/46<br>14/19D | 7(a), 16 | |
| (b) Consistency | 38/46<br>14/19D | 7(b), 16 | |
| (c) Accrual | 38/46<br>14/19D | 7(c), 16 | |
| (d) Prudence (however, creation of secret or hidden reserves is not justified) | 38/46<br>14/19D | 9(a), 17 | |
| 2. Income smoothing (considered undesirable in most countries, but frequently found in 12 of 24 countries separately surveyed) a/ | | | |
| General provisions (and subsequent reversals) are used to shift income between periods, for example: | | | |
| (a) Unwarranted general provisions for doubtful accounts receivable | | | |
| (b) Special inventory write-downs | | | |
| (c) Additional depreciation for certain categories of fixed assets and replacement reserves in addition to normal depreciation | | | |
| (d) Overprovision for contingencies | | Agenda | |
| 3. Historical cost<br>While not universally applied, departures are disclosed as a reporting standard. | No. 9<br>37/46<br>12/19D | IAS 1, 13 (Also implied in IAS 2, 1 and 2) | |
| 4. Accounting for the effects of inflation | Various and none. Nos.10-16 | ED 5<br>A single method not selected | |

| | | Practice survey | IASC | OECD-GL |
|---|---|---|---|---|
| 5. | Equity accounting for significant investments in associated companies | No. 105<br>9/46<br>5/19D | IAS 3 | |
| 6. | Line of business reporting: | | | |
| | (a) Sales | No. 255<br>8/38<br>4/19D | Agenda | b/<br>(iii) |
| | (b) Profits | No. 256<br>0/46<br>0/19D | Agenda | (iv) |
| | (c) New capital | Not surveyed. Infrequently found. | | |
| 7. | Social performance | | | |
| | (a) Profit | Not surveyed as such | | |
| | (b) Wages and salaries | Not surveyed | | |
| | (c) Training (wages and expenses) | Not surveyed | | |
| | (d) Number of employees | Not surveyed | | |
| | (e) Pensions | (Nos. 166-175<br>( | | |
| | (f) Service and severance indemnities | (Various principles | | |
| | (g) Contributions | Not surveyed | | |
| | (h) Investment grants | No. 58<br>7/16<br>5/13D | | |
| | (i) Fixed assets or portions purchased, modified, dismantled or abandoned for:<br>Pollution control<br>Safety and health<br>Beautification | Not surveyed | | |
| | (j) Increased processing costs incurred for:<br>Pollution control<br>Safety and health<br>Beautification | Not surveyed | | |

| | Practice survey | IASC | OECD-GL |
|---|---|---|---|
| (k) Disclosures in the form of descriptive prose and opinion regarding efforts to improve the "quality of life". | Not surveyed. Infrequently found. | | |
| 8. A statement of the source and use of funds by an enterprise as a whole is a basic financial statement. | No. 205<br>9/46<br>4/19D | ED 7 | (v) |
| The following concepts apply primarily to the home country consolidated financial statements of a transnational corporation. | | | |
| 9. Geographical reporting: | Not surveyed | IAS 3, 47(e) | c/ |
| (a) Assets | Various principles | | |
| (b) Sales | Infrequently found | | (iii) |
| (c) Profit | | | (iii) |
| (d) New capital | | | (iv) |
| (e) Average number of employees | | | (vi) |
| (f) Describe principal activities | | | (ii) |
| (g) Line of business reporting | (See 6 above) | | (see 6 above) |
| 10. Consolidation, including foreign subsidiaries (Elimination of the effect on consolidated income of inter-company transactions assumed) | Nos. 210-211<br>24/46<br>9/19D<br>Various principles<br>Nos. 207-232 | IAS 3 (describes many related accounting principles) | |
| 11. Translation of foreign accounts | Various principles<br>Nos. 233-238 | Agenda | |

(Note and foot-notes on following page)

(Note and foot-notes to table)

Note: Studies of items 4. Accounting for the effects of inflation; 6. Line-of-business reporting (segment of a business); 7. Social performance; 9. Geographical reporting; and 11. Translation of foreign accounts are not likely to lead to general acceptance of a standard supported by definitive accounting principles or reporting requirements in the near future. Further comments are made elsewhere on each of these items.

a/ Guide for the Reader of Foreign Financial Statements, George C. Watt, editor, Price Waterhouse and Co., USA, 1975.

b/ For the enterprise as a whole.

c/ Groups of countries or individual countries as appropriate, considering, among other things, the effects on competitiveness.

## C. Accounting principles

| | | Practice survey | IASC | OECD-GL |
|---|---|---|---|---|
| | The following investments are carried on an equity basis: | | | |
| 1. | 50 per cent owned companies | No. 103<br>10/46<br>5/19D | IAS 3<br>4, 40 | |
| 2. | Joint ventures | No. 104<br>9/46<br>5/19D | IAS 3<br>4, 40 | |
| 3. | Less than 50 per cent owned companies significantly influenced | No. 105<br>9/46<br>5/19D | IAS 3<br>4, 40 | |
| 4. | When an investment is accounted for on the equity basis, practices similar to those in consolidation are followed. | No. 106<br>17/46<br>8/19D | IAS 3,<br>25 | |
| 5. | Goodwill arising on acquisition of a subsidiary or a business is amortized against earnings over the period estimated to be benefited (usually not to exceed 40 years). | No. 221<br>9/46<br>5/19D | | |
| 6. | Business combination - Description of a pooling of interests or merger.<br>If a business combination is effected by an exchange of shares, it is accounted for as a pooling of interests (merger) provided the substance of the main business of the constituent companies continues, and the combination results from an offer to equity voting shareholders, and the offer is accepted by not less than 90 per cent of the total equity voting capital of the company or companies receiving the offer (no size test). | No. 239<br>8/38<br>6/19D | | |

| | | Practice survey | IASC | OECD-GL |
|---|---|---|---|---|
| | The following concept applies primarily to the home country consolidated financial statements of a transnational corporation. | | | |
| 7. | Consolidations - Determination of the amount of purchased goodwill. The excess of the cost of acquiring a company over the total of the book amounts of the net assets acquired is assigned to the tangible and identifiable intangible assets (e.g. patents) and to liabilities on the basis of their fair values at the date of acquisition and any unassigned amount is recorded as goodwill. | No. 219<br>17/46<br>6/19D | IAS 3<br>13 | |

Note: These accounting principles are mostly, but not entirely applicable to the consolidated financial statements of a transnational corporation. IAS 3 deals with many of them and further applications are vital to harmonization.

## D. Reporting standards

| | | Practice survey | IASC | OECD-GL |
|---|---|---|---|---|
| 1. | Significant accounting policies used are disclosed. | No. 17<br>24/46<br>10/19D | IAS 1<br>18 | (ix) |
| 2. | Comparative financial statements are issued. | No. 22<br>34/46<br>14/19D | IAS 1<br>21 | |
| 3. | The effect of a change in accounting principles or methods is disclosed. | No. 18<br>34/46<br>12/19D | IAS 1<br>22 | |
| 4. | Any variations (whether or not a change) from historical cost are disclosed. | No. 9<br>37/46<br>12/19D | IAS 1<br>13 | |
| 5. | Interests of directors in contracts are disclosed in financial statements or in accompanying documents (e.g. directors' reports). | No. 261<br>10/46<br>5/19D | | |
| | The following concept applies primarily to the home country consolidated financial statements of a transnational corporation. | | | |
| 6. | Structure of the enterprise is disclosed: | Not surveyed | IAS 3 | (i) |
| | (a) Name and location of parent. | | IAS 3<br>47 | (i) |
| | (b) Name and location of main subsidiaries consolidated, subsidiaries not consolidated, and associated companies. | | IAS 3<br>47 | (i) |
| | (c) Percentage owned. | Not surveyed | | (i) |
| | (d) Share capital of parent held by subsidiary companies. | No. 213<br>16/27<br>10/19D | | (i) |

Note: These reporting standards are basic to disclosures at all levels of reporting. IAS 1 deals with many of them and further applications are vital to harmonization.

## E. Disclosure of accounting policies

| | | Practice survey | IASC[a] | OECD-GL[b] |
|---|---|---|---|---|
| (All companies) | | | | |
| 1. | Events subsequent to the balance sheet date. | No. 152<br>29/46<br>14/19D | IAS 1<br>13 | |
| 2. | Leases. | No. 53<br>12/46<br>5/19D | IAS 1<br>13 | |
| 3. | Taxes. | Not surveyed[c] | IAS 1<br>13 | |
| 4. | Long-term contracts. | Not surveyed | IAS 1<br>13 | |
| 5. | Inventories: | | | |
| | Basis of carrying disclosed. | No. 77<br>32/46<br>11/19D | IAS 2<br>34 | |
| | Basis (FIFO, LIFO, average, etc.) disclosed. | No. 88<br>19/46<br>6/19D | | |
| 6. | Fixed assets. | No. 23<br>33/46<br>9/19D | ED 4<br>27 | |
| 7. | Depreciation. | No. 64<br>24/46<br>11/19D | ED 4<br>20 | |
| 8. | Research and development. | Not surveyed | IAS 1<br>13 | |
| 9. | Patents and trademarks. | Not surveyed | IAS 1<br>13 | |
| 10. | Warranties. | Not surveyed | IAS 1<br>13 | |
| 11. | Commitments | Not surveyed | IAS 1<br>13 | |

| | Practice survey | IASC | OECD-GL |
|---|---|---|---|
| 12. Contingencies. | Not surveyed | IAS 1<br>13 | |
| 13. Pension costs and retirement plans. | Not surveyed | IAS 1<br>13 | |
| 14. Severance and redundancy payments. | Not surveyed | IAS 1<br>13 | |
| 15. Methods of revenue recognition. | Not surveyed | IAS 1<br>13 | |
| 16. Maintenance, repairs and improvements. | Not surveyed | IAS 1<br>13 | |
| 17. Gains and losses on disposals of property. | Not surveyed | IAS 1<br>13 | |
| 18. Reserve accounting (is not used). | Not surveyed | IAS 1<br>13 | |
| 19. Direct charges and credits to surplus accounts. | Not surveyed | IAS 1<br>13 | |
| (The following disclosures are essential in reports of transnational corporations, although they were not specifically set out in IAS 1.) | Not surveyed. Various principles | | |
| 20. Method of determining transfer prices.)<br>)<br>21. Method of determining the cost of )<br>items transferred. ) | Not surveyed | Not an agenda item | (viii) (under study) |
| 22. Method of determining the geographical<br>(a) Spread of assets.<br>(b) Source of revenue.<br>(c) Source of gross profit. | Not surveyed | Not an agenda item | |

(Notes and foot-notes on following page)

(Notes and foot-notes to table)

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Notes: The descriptions of accounting principles suggested in IAS 1 are ample as a guideline. While applications were not surveyed in depth, it is apparent that current practice does not measure up to this standard, even in developed countries. Substantial improvement in this area at an early date can only be expected if national professional organizations and regulatory agencies of governments act soon to require these disclosures. Simple disclosure of the fundamental concepts and accounting principles and methods applied will not cause any serious problems of implementation for issuers of financial statements.

Items 20 and 21 involve matters related to taxation and have been important to regulatory agencies of governments for many years. Only recently have they been recognized as important to the information reported by transnational corporations in reports to their shareholders and the public. Item 22, which relates to geographical information reported by transnational corporations, involves principles in items 20 and 21, but also calls for a choice between principles suited to management control and analysis, or principles based on risk of loss of foreign investments (subsidiaries and associated companies).

a/ IAS 1, paragraph 13, tabulates areas where diverse accounting policies are applied, possibly producing significantly different results. It is implied that harmonization can be expected to take time, and that immediate improvement is possible if the particular concepts, principles and practices applied by an issuer of financial statements are disclosed. IAS 1, para. 18, calls for "disclosure of all significant accounting policies".

b/ Guidelines for Multinational Enterprises (OECD) calls for disclosure of "the accounting policies, including those on consolidation, observed ...".

c/ The study referred to in foot-note a/ of section B above established that various accounting principles and practices were applied with respect to this item and items 4 and 8 to 19. The existence of various accounting principles and practices reinforces the need for these areas to be categorized as requiring a description of the particular accounting principle applied.

## II. SUPPORTIVE ACCOUNTING PRINCIPLES AND REPORTING PRACTICES

### A. Accounting principles

| | | Practice survey | IASC |
|---|---|---|---|
| (All companies) | | | |
| 1. | All known liabilities are recorded regardless of whether their definite amount is determinable. | No. 113<br>45/46<br>18/19D | |
| 2. | Where accounting income differs from taxable income, except for permanent differences, a provision for deferred taxes is recorded (comprehensive tax allocation). Not considered a desirable practice by many. | No. 189<br>8/46<br>7/19D | Agenda |
| 3. | Liabilities existing at the balance sheet date for pension rights vested in employees are recorded in the financial statements. | No. 168<br>14/46<br>7/19D | |
| 4. | Investments in marketable securities classified as current assets are carried at the lower of cost and market value. | No. 107<br>34/46<br>16/19D | |
| 5. | Investments classified as long-term which are carried at cost are written down by a provision for any impairment in value. | No. 110<br>31/46<br>14/19D | |
| 6. | Cost of inventories includes direct material and labour and all variable and fixed manufacturing overheads (may be based on the capacity of the facilities). | No. 91<br>34/46<br>12/19D | IAS 2[a/] |
| 7. | Inventories are carried at cost or market whichever is lower. | No. 79<br>41/46<br>17/19D | IAS 2<br>32 |
| 8. | Charges to income are made in a systematic and rational manner for depreciation of all types of depreciable assets, including non-industrial buildings (e.g. offices, hotels, etc.). | No. 59<br>36/46<br>13/19D | ED 4<br>22 |

| | | Practice survey | IASC |
|---|---|---|---|
| 9. | Costs of construction of fixed assets include direct material and labour and an appropriate portion of overhead. | No. 29<br>30/46<br>10/19D | |
| 10. | Basis on which fixed assets are stated. | Various principles | |
| 11. | Fixed assets are written down (other than by depreciation) if their value to the business is lower than cost less accumulated depreciation. | No. 28<br>25/46<br>15/19D | |
| 12. | Discount on an issue of long-term debt is amortized over the term of the debt by the interest method, i.e., based on the outstanding principal balance and not the straight-line method. | No. 126<br>12/46<br>4/19D | |
| 13. | Research and development. | Various principles | Agenda |
| 14. | Accounting for long-term contracts. | Various principles | Agenda |
| 15. | Any shares of a company's own stock reacquired are recorded at cost and shown as a reduction of shareholders' equity. | No. 130<br>16/46<br>5/19D | |
| 16. | Capital gains (other than those resulting from transactions in the company's own shares) are reported in the income statement. | No. 139<br>32/46<br>15/19D | |
| 17. | Provision is made for anticipated losses on unexpired purchase contracts. | No. 157<br>27/46<br>13/19D | |

(The following principles are essential in reports of transnational corporations, although they have not been added to the agenda of IASC.)

18. Determining transfer prices

(a) Price to an unrelated party.

| | Practice survey | IASC |
|---|---|---|
| (b) Cost. | | |
| (c) Cost plus. | | |
| 19. Determining the cost of items transferred | | |
| (a) Allocation of manufacturing overhead to lines of business. | | |
| (b) Allocation of service centre costs to lines of business or other service centres. | | |
| (c) Allocation of general and administrative expenses to lines of business. | | |
| 20. Allocation of research and development - geographically. | | |
| 21. Allocation of home office expenses - geographically. | | |
| 22. Geographical spread of assets. | | |
| (a) Risk basis, or | | |
| (b) Employed by the segment. | | |
| 23. Geographical spread of revenue | | |
| (a) Location of customer, or | | |
| (b) Location of last significant manufacturing effort. | | |
| 24. Geographical spread of gross profit | | |
| (a) Location of raw material, or | | |
| (b) Location of customer, or | | |
| (c) Location of last significant effort. | | |

(Notes and foot-note on following page)

(Notes and foot-note to table)

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Notes: The accounting principles listed under I B above are basic principles dealing with the structure of the reporting entity of a transnational company. The amounts reported are influenced by the principles in this section. These principles also apply to the financial statements issued by a member (subsidiary or associate) of the enterprise (group).

Item 2. While accounting for income taxes is on the agenda of IASC, formulation of an accounting principle gaining early general acceptance in the near future is not likely. In the United States, where such a principle was first required in 1967, considerable disagreement remains over comprehensive income tax allocation.

Item 3. Employment costs, including pensions, disability payments and severance indemnities, are a large part of value added by an enterprise. This should warrant an effort to develop an international standard. The vast differences in labour laws in various countries will make for a complex study if the standard is to accommodate various circumstances.

Item 10. The practice survey shows that various principles are applied to fixed assets. The resolution of this matter can only be considered after agreement on a Fundamental Accounting Concept (item 4, section B, Accounting for the effects of inflation).

Item 12. Surprisingly, the practice survey shows that little consideration is given to the cost of money concept. Not only is interest amortized on the straight-line method even when the principal is reduced periodically, but it is probable that no "imputed" cost is attached to an interest-free loan. This principle deserves attention - it is close to being a fundamental concept.

a/ Permits exclusion of overhead if that fact is disclosed.

## B. Reporting practices

| | Practice survey | IASC | OECD-GL |
|---|---|---|---|
| The reporting standards listed in section I D above are general. The reporting practices in this section are most important in establishing compliance with the general standards. For convenience in evaluating future practice, the items below are listed from a June 1975 exposure draft of IASC. | | | |
| DISCLOSURES | | | |
| BALANCE SHEET (disclosures) | | | |
| <u>General</u> | | | |
| 1. Restrictions on the title to assets | No. 153<br>27/46<br>10/19D | ED 5<br>14a | |
| 2. Security given in respect of liabilities. | No. 116<br>35/46 | ED 5<br>14b | |
| 3. Contingent assets. | Not surveyed | ED 5<br>14c | |
| Contingent liabilities. | No. 118<br>37/46<br>15/19D | ED 5<br>14c | |
| 4. Contracts for future capital expenditure. | No. 45<br>25/46<br>8/19D | ED 5<br>14d | |
| 5. Methods of providing for pension and retirement plans (and) how the liabilities arising are provided for. | Not surveyed | ED 5<br>16 | |
| <u>Property, plant and equipment</u> | | | |
| 6. Acquisitions during the period | No. 39<br>16/46<br>6/19D | ED 5<br>19 (a) | |

| | | Practice survey | IASC | OECD-GL |
|---|---|---|---|---|
| 7. | Disposals during the period. | No. 39<br>16/46<br>6/19D | ED 5<br>19 (b) | |
| 8. | Accumulated depreciation at the end of the period. | No. 39<br>16/46<br>13/19D | ED 5<br>19 (c) | |
| 9. | Not in use. | No. 41<br>9/46<br>13/19 | ED 5 | |
| Other long-term assets | | | | |
| 10. | If applicable, the method and period of amortization and any unusual write-offs during the period (such as): | | | |
| | (a) Goodwill. | Not surveyed | ED 5<br>21 (d) | |
| | (b) Patents, trademarks, etc. | No. 151<br>38/46<br>16/19D | ED 5<br>21 (e) | |
| | (c) Expenditures carried forward (such as) | | ED 5<br>21 (f) | |
| | (d) Research and development. | No. 186<br>18/46<br>5/19D | Agenda | |
| | (e) Preliminary expenses. | Not surveyed | | |
| | (f) Reorganization expenses. | Not surveyed | | |
| | (g) Deferred taxes. | Not surveyed | Agenda | |
| Current assets | | | | |
| 11. | Cash not immediately available. | Not surveyed | ED 5<br>22 (a) | |
| 12. | Market value of marketable securities. | No. 108<br>29/46<br>9/19D | ED 5<br>22 (b) | |

| | | Practice survey | IASC | OECD-GL |
|---|---|---|---|---|
| 13. | Intercompany receivables. | No. 114<br>34/46<br>15/19D | ED 5<br>22 (c) | |
| Long-term liabilities | | | | |
| 14. | Interest rates, repayment terms, conversion features and amounts of unamortized premium or discount. | No. 125<br>26/46<br>8/19D | ED 5<br>23 | |
| 15. | Intercompany loans. | No. 121<br>34/46<br>15/19D | ED 5<br>23 | |
| INCOME STATEMENT | | | ED 5<br>27 | |
| At least the following ... | | | | |
| 16. | Sales or other operating revenue. | No. 160<br>34/46<br>15/19D | | |
| 17. | Depreciation. | No. 65<br>41/46<br>17/19D | | |
| 18. | Interest income and expense. | Not surveyed | | |
| 19. | Income from investments. | Not surveyed | | |
| 20. | Taxes on income. | No. 187<br>38/46<br>15/19D | | |
| 21. | Unusual charges or credits. | No. 197<br>35/46<br>13/19D | | |
| 22. | Significant intercompany transactions. | Not surveyed | | |
| 23. | Net income. | No. 199<br>44/46<br>19/19D | | |

| | | Practice survey | IASC | OECD-GL |
|---|---|---|---|---|
| Other | | | | |
| 24. | For each major class of depreciable assets, the useful lives or depreciation rates used. | Not surveyed | ED 4<br>27 (c) | |
| 25. | Research and development expenditure. | | Agenda | (vii)[a] |
| 26. | Past service pension costs not provided for are disclosed. | No. 170<br>15/46<br>6/19D | | |
| 27. | Where accounting income differs from taxable income, deferred taxes are not recorded but are shown in a foot-note to the financial statements. | No. 190<br>4/43<br>1/19D | Agenda | |
| 28. | Commitments (amounts and periods) for future years under leases and hire purchase contracts are disclosed. | No. 52<br>11/46<br>4/19D | | |
| 29. | The rights and preferences of shareholders to dividends and to principal are disclosed. | No. 129<br>33/46<br>13/19D | ED 5<br>26 (a) | |
| 30. | Restrictions on distribution of retained earnings (because of trust deeds, bank loan agreements or legal restrictions) are disclosed. | No. 140<br>22/46<br>9/19D | ED 5<br>26 (b) | |
| 31. | Statutory financial statements are prepared in accordance with an official format. | No. 264<br>16/46 | | |

(Notes and foot-note on following page)

(Notes and foot-note to table)

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Notes: Exposure draft 5 calls for 36 other balance sheet classifications not listed above and considered to be ample to illustrate items that should be disclosed separately, if significant. All the specific disclosures established by ED 5, paras. 14-27, are reproduced in annex IX.

The disclosure of items 16-23 only will not accommodate "value added" type analysis.

Substantial improvement in this area may be expected at an early date only if national professional organizations and regulatory agencies of governments act soon to require these disclosures. There are no serious implementation problems for issuers of financial statements in simply disclosing the information and/or amounts.

The disclosures set forth in IASC ED 5 are adequate. It is expected that, as various areas of accounting are the subject of individual statements (standards) set by the IASC, other disclosures will be established.

a/ For the enterprise as a whole.

## Annex II

## CONFIDENTIAL REPORTS TO THE UNITED STATES GOVERNMENT: INWARD AND OUTWARD FOREIGN INVESTMENT

### A. Department of Commerce, Bureau of Economic Analysis

#### Survey of foreign direct investment in the United States (year 1974) (form BE-12)

Under the Foreign Investment Study Act of 1974 the Department of Commerce was directed to survey direct foreign investments in the United States of over 10 per cent of voting rights of an entity or of ownership of real estate. Consolidated reports may be filed (domestic consolidation only).

Information to be filed includes:

(1) Percentage of foreign ownership of the United States company and claims on and debts to the foreign investor and other foreign persons. The foreign investor is identified by country of residence;

(2) Equity transactions between the foreign investor and the United States company and share of the net income of the United States company;

(3) Schedule of receipts and payments of dividends, interest, fees, royalties and rentals between the foreign investor and the United States company;

(4) Merchandise trade (exports/imports) with: the foreign investor; other foreigners;

(5) Percentage of total net sales by over 100 major classifications;

(6) Financial statement data of the United States company;

(7) Supplementary (total) data by States, covering:

Number of employees

Wages and salaries

Net sales

Total property plant and equipment owned by 16 classifications

Annual lease commitments for property, plant and equipment.

## B. Department of the Treasury

### Survey of foreign portfolio investments in the United States (1974 - last previous, 1941) (forms FPI-1, FPI-2)

The Foreign Investment Study Act of 1974 also directed this Department to survey direct foreign portfolio investments in the United States - investments in debt securities and investments of less than 10 per cent of voting rights or of ownership in real estate. Consolidated reports may be filed (domestic consolidation only).

Information to be filed includes:

(1) Foreign ownership interest in the United States company's:

Equity securities

Long-term debt obligations

Real estate. The foreign investor is identified by country of residence;

(2) Identity of the United States securities exchanges on which the United States company's shares are traded;

(3) Identity of the securities exchanges outside the United States on which the shares are traded;

(4) From the annual report to shareholders:

Total assets

Total liabilities

Sales

Net earnings

(Full consolidation of foreign subsidiaries).

## C. Department of Commerce, Bureau of Economic Analysis

### Survey of United States business investments in foreign countries (form BE-10)

The most recent survey was for the year 1966. Prior surveys were made for the years 1957, 1950, 1940, 1936 and 1929 and a survey is expected in 1976. Each United States company must report, but consolidated reports may be filed (for parent and United States subsidiaries but excluding any such company operating mainly abroad).

For the United States company, the form calls for the following information:

(1) Total assets

(2) Total liabilities

(3) Foreign assets in (1) above

(4) Foreign liabilities in (2) above

(5) Net income

(6) Research and development expenditures

(7) Exploration and development expenditures (natural resources).

A separate BE-10 is filed for each foreign subsidiary. The information to be filed includes:

(1) A balance sheet, "based on the books of the foreign organization and stated in the currency in which the books are kept. If the accounts are already converted to United States dollars, give the amounts in United States dollars only and in the space provided for ... no conversions are required. If conversions are made, specify the methods used in converting";

(2) Property, plant and equipment, for foreign oil and mining organizations only;

(3) Income statement;

(4) Surplus reconciliation for the year;

(5) United States company's equity in net income;

(6) Net income of foreign branches or properties;

(7) Sales in (3) above analysed as to:

| | Total | Inter-company | Outside |
|---|---|---|---|
| Local | | | |
| Exports back to the United States | | | |
| Exports to other countries; | | | |

(8) Sales by major products or services;

(9) Research and development (whether capitalized or expensed);

(10) Payroll costs:

Wages

Salaries

Supplementary benefits;

(11) Employees:

Wage earners

Salaried

| | United States | Other |
|---|---|---|
| Managerial | | |
| Professional or technical | | |
| Other salaried; | | |

(12) Imports of the foreign subsidiary in 1966:

Capital equipment imported -

From the United States

From other countries

Other imports, total -

From the United States

From other countries;

(13) Statement of the source and use of funds;

(14) Investment of United States (reporting) company:

Current liabilities owed to United States company

Long-term debt owed to United States company

Common and preferred stock owned by United States company

United States company's equity in capital and earned surplus

Home office account;

(15) Investment of foreign subsidiary in United States company;

(16) Receipts and payments by United States company:

Cash dividends

Interest

Royalties, licence fees, etc.

Rentals for use of tangible property

Charges for services, allocated expenses, etc.;

(17) All United States goods charged to the foreign subsidiary on the United States company books:

By ultimate destination

Export shipments to the country in which subsidiary is organized

Export shipments to United States company subsidiaries in all other countries

Export shipments to non-affiliated residents of all other countries

| Products of United States company | Products of other United States suppliers a/ |
|---|---|

(18) Similar data to (17) for United States goods consigned;

(19) All United States goods actually shipped:

By type of goods -

For processing or assembly -

Parts, components or other manufactured goods

Crude or unmanufactured materials or supplies

For resale without further manufacturing -

Manufactured goods

Crude or unmanufactured

For lease or rental -

Capital equipment and machinery

Other purchases of United States goods;

(20) Information in (17), (18) and (19) above, summarized by countries.

a/ Run through the books of the United States company.

## Annex III

### CONFIDENTIAL REPORTS TO THE UNITED STATES GOVERNMENT: BALANCE-OF-PAYMENTS ITEMS

### A. Department of Commerce, Bureau of Economic Analysis

The following reports deal with the balance of payments. Following the issuance of FAS 8 by the Financial Accounting Standards Board, all monetary balances must be translated at the current rate of exchange after 1975. Accounting standards influence only the determination of the net income and net worth of foreign subsidiaries, where that information is required to be reported.

1. Transactions with foreign subsidiary or affiliated corporations (form BE-577)

A separate BE-577 is filed for each foreign subsidiary and each foreign affiliated (25 to 49 per cent owned) company. Information under items 1 to 9 is to be filed quarterly, under items 10 and 11 annually. A consolidated report may be filed (for parent and United States subsidiaries but excluding any such company operating mainly abroad).

The information to be filed includes:

(1) Investment movement

(2) Intercompany account balances

(3) Dividends

(4) Interest

(5) Royalties, management fee, allocated expenses, etc.

(6) Net income (for the quarter)

(7) Net income for the year (United States company's equity)

(8) Equity in net worth, showing:

Capital stock

Capital and earned surplus

Surplus reserves.

2. Transactions of primary foreign organizations with secondary foreign organizations (form BE-577S, filed annually)

The information required is the same as for BE-577, described above.

3. Transactions with associated foreign enterprises (10 to 25 per cent owned) (form BE-577A, filed annually)

The information required is the same as for BE-577, described above.

4. Operations of foreign branches (form BE-578, filed quarterly)

The report analyses changes in net investment.

5. International receipts and payments of royalties, licensing fees, rentals, etc. (form BE-93, filed annually)

This report covers receipts and payments from and to non-affiliated foreign companies.

6. Transactions with foreign parent (form BE-605, filed quarterly)

The purpose of this form is to provide information on direct-investment operations of foreign persons or firms in the United States that affect the United States balance of international payments.

The information required includes:

(1) Items paid or credited to foreign parent;

Dividends (after withholding tax);

Interest on bonds, notes, advances, etc.;

Royalties, license fees, and rentals;

Charges for management, services, head-office expenses, allocated, etc.

(2) Net income and retained earnings;

Foreign parent's equity in net income;

Foreign parent's equity in the retained earnings of the United States company (annually only).

(3) Intercompany accounts with foreign parent and its foreign affiliates;

| | Payable by US Co. | Due to US Co. |
|---|---|---|
| Beginning, and ending | | |

Changes in holdings of capital by foreign parent.

7. Transactions of United States branches (form BE-606)

This form is similar to BE-605 but is designed for branch accounts rather than accounts of a subsidiary.

## B. Federal Reserve Bank

The following reports deal with balance-of-payments positions (not movements). A consolidated report may be filed (for parent and United States subsidiaries but excluding any such company operating mainly abroad, the latter being regarded as a foreign reporter).

1. Short-term liquid claims on foreigners (non-affiliates) (form C-3, filed monthly)

This form reports in United States dollars the bank balances, time deposits and certificates of deposit balances held in foreign countries for the account of domestic companies reporting. The report is broken down by foreign countries.

2. Short-term liquid claims on foreigners in countries not listed separately on form C-3 (form C-4, filed annually)

Filed as of 30 September, this form lists by country and amount the balances which were reported on form C-3 for September as "All other countries".

3. Liabilities to, and claims on, foreigners (non-affiliates) (form C-1/2, filed quarterly)

Reports in United States dollars foreign receivables and payables, broken down by foreign countries, and classified as to short-term and long-term.

4. Foreign currency positions (domestic reporters) (form FC-3, filed monthly if volume requires it, otherwise quarterly)

Reports in foreign currency, in nine specified foreign currencies:

(1) Assets;

(2) Liabilities;

(3) Forward exchange open contracts;

(4) Net over-all position.

Reporters are United States non-banking business concerns.

5. Foreign currency positions (foreign reporters) (form FC-4, filed quarterly)

United States non-banking business concerns report for all their foreign subsidiaries and partnerships. Incidentally, this report also covers United States branches and United States subsidiaries of foreign non-banking concerns.

Reports in foreign currency <u>and in United States dollars</u> in nine specified foreign currencies the information described above under FC-3.

6. <u>Purchases and sales of long-term securities by foreigners</u> (form S-1, filed monthly)

It reports in United States dollars the long-term securities of the United States company purchased from or sold to non-affiliated foreigners, unless the transaction was made through a broker in securities.

Annex IV

# CONFIDENTIAL REPORTS TO THE UNITED STATES GOVERNMENT: INDUSTRIAL CENSUS

## A. Department of Commerce, Bureau of the Census

The information required concerns primarily domestic economic matters. Consolidated assets include only the net investment in foreign branches or foreign subsidiaries. Where sales values are analysed between United States and foreign destinations, the emphasis is still on the value of total goods produced domestically.

### 1. Report of organization (form NC-XIA, filed annually)

Reports each domestic plant, showing street address, majority activity by 4-digit SIC code number, census file number (10-digit), employer identification number (9-digit), number of employees and payroll amounts, and status at the end of the year (operating, inactive, sold, closed, etc.)

### 2. Annual survey of manufactures (form MA-100)

The survey is designed to produce reports providing the following:

(1) General statistics (employment, payrolls, man-hours, value added by manufacture, cost of materials, value of shipments and capital expenditures) for industries and industry groups and geographical divisions, states, large standard metropolitan statistical areas, large counties and selected cities by major industry groups.

(2) Value of shipments for classes of products (quantity of shipments data to be provided for selected classes).

(3) Expenditures for new plant and new equipment at manufacturing establishments in operation and under construction for industry groups and states.

(4) Value of inventories of finished products, work-in-process, and materials for industry groups and industries.

(5) Fuels and electricity data for industry groups and states.

(6) Value of assets and rental payments for industries, states, and large standard metropolitan statistical areas.

(7) Employment and labour costs for operating manufacturing establishments for industries and states.

Shipments are classified by the SIC code numbers (5-digit).

The items on the report form are as follows:

| | |
|---|---|
| Item 1. | Physical location and employer identification number |
| Item 2. | Number of employees |
| Item 3A. | Payrolls |
| Item 3B. | Supplemental labour cost |
| Item 4. | Plant man-hours of production workers, by quarter |
| Item 5. | Cost of materials, fuels, electricity, contract work |
| Item 6. | Inventories of this establishment at end of year |
| Item 7. | Capital expenditures during year (exclude land) |
| Item 8. | Quantity of electricity |
| Item 9. | Quantity and value of products shipped and other receipts |
| Item 10. | Value of fixed assets |
| Item 11. | Rental payments |
| Items 13-14. | Change in operator or organization and company affiliation. |

3. Survey of industrial research and development (form RD-1, filed annually)

Reports all domestic R and D expenditures in connexion with:

(1) Basic research;

(2) Applied research;

(3) Development.

Also requires information as to number of man-years, field of basic research, product grouping of applied research, R and D by states, pollution abatement expenditures, etc.

4. Survey on pollution abatement costs and expenditures (form MA-200, filed annually)

These reports were initiated in 1973. The survey provides for quantitative measurement of air pollutants and solid wastes dispersed by abatement efforts. Requires the capital expenditures and operating costs for pollution abatement:

(1) Depreciation;

(2) Equipment leasing;

(3) Labour;

(4) Materials and supplies;

(5) Services;

(6) Other costs.

5. <u>Form 1972 economic census - censuses of business, manufactures and mineral industries</u>

The census (taken at five-year intervals) is basically an enlargement of the Annual Survey of Manufactures.

## B. Federal Trade Commission

1. Corporate patterns survey (forms CPR-1, corporate patterns reports - 1972, CPR-2, CPR-3, applicable to the largest domestic manufacturing companies)

The Federal Trade Commission last conducted a corporate patterns survey in 1950, but the present intention is to conduct the survey on a regular basis at five-year intervals. The information is to remain confidential for three to five years. The Commission would furnish individual company data in response to a request by a congressional committee or pursuant to a court order. Litigation continues to block these reports.

The three basic forms utilized in the corporate patterns report survey are the following:

CPR-1 - Primary reporting form, requiring data on a company's domestic operations

CPR-2 - Secondary reporting form, requiring information on joint ventures and less than 50 per cent-owned subsidiaries

CPR-3 - Screening form for "borderline" firms which may rank among the country's 1,000 largest

The reports require primarily information relative to "value of shipments" for domestic manufacturing activities by five-digit SIC code for the calendar year 1972. CPR-1 requires a list and description of all subsidiaries, joint ventures and other ownership interest, segregated between over 50 per cent and 5 to 50 per cent-owned.

There are certain basic differences between the corporate patterns survey and the line of business programme, as follows:

| | Corporate patterns survey | Line of business programme |
|---|---|---|
| Period covered | 1972 | 1974 |
| Number of companies required to report | 1,100 (approx.) | 450 |
| Transfer pricing basis | Economic (market) value | Book value |
| Product class relief for vertical integration | No | Yes |
| Assets and profits reporting | Total company only | By line of business |

2. Line of business report (form LB - applicable to the largest domestic manufacturing companies)

In connexion with line-of-business reporting, the Federal Trade Commission has stated, in part:

> As the activities of previously specialized companies were integrated into the organization of large conglomerate corporations it has become increasingly difficult to obtain a clear picture of financial developments in specific industries.
>
> "Second, the Federated Trade Commission has made a vigorous effort in recent years to improve the effectiveness of its law enforcement resource allocations for antitrust and consumer protection.
>
> "Schedule III, the heart of the revised LB questionnaire, is designed to elicit information vitally needed in evaluating industry performance. Gross margin, contribution margin, and operating income figures measure various dimensions of price structure and profitability, with important implications for the efficiency with which markets allocate resources to meet consumer demands."

## Annex V

EXCERPT FROM THE ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT: GUIDELINES FOR MULTINATIONAL ENTERPRISES

"DISCLOSURE OF INFORMATION

"Enterprises should, having due regard to their nature and relative size in the economic context of their operations and to requirements of business confidentiality and to cost, publish in a form suited to improve public understanding a sufficient body of factual information on the structure, activities and policies of the enterprise as a whole, as a supplement, in so far as is necessary for this purpose, to information to be disclosed under the national law of the individual countries in which they operate. To this end, they should publish, within reasonable time-limits, on a regular basis, but at least annually, financial statements and other pertinent information relating to the enterprise as a whole, comprising in particular:

"(i) The structure of the enterprise, showing the name and location of the parent company, its main affiliates, its percentage ownership, direct and indirect, in these affiliates, including shareholdings between them;

"(ii) The geographical areas* where operations are carried out and the principal activities carried on therein by the parent company and the main affiliates;

"(iii) The operating results and sales by geographical area and the sales in the major lines of business for the enterprise as a whole;

"(iv) Significant new capital investment by geographical area and, as far as practicable, by major lines of business for the enterprise as a whole;

"(v) A statement of the sources and uses of funds by the enterprise as a whole;

---

"* For the purposes of the guidelines on disclosure of information the term 'geographical area' means groups of countries or individual countries as each enterprise determines is appropriate in its particular circumstances. While no single method of grouping is appropriate for all enterprises, or for all purposes, the factors to be considered by an enterprise would include the significance of operations carried out in individual countries or areas as well as the effects on its competitiveness, geographic proximity, economic affinity, similarities in business environments and the nature, scale and degree of interrelationship of the enterprises' operations in the various countries."

"(vi) The average number of employees in each geographical area;

"(vii) Research and development expenditure for the enterprise as a whole;

"(viii) The policies followed in respect of intra-group pricing;

"(ix) The accounting policies, including those on consolidation, observed in compiling the published information."

Annex VI

## INTERNATIONAL ACCOUNTING STANDARDS COMMITTEE:[a/] AGENDA[b/]

| | | Expected date of approval for publication | | |
|---|---|---|---|---|
| | | Exposure draft | Definitive standard | Steering Committee members |
| 1. | Disclosure of Accounting Policies | January 1974 (issued) | November 1974 (approved) | France<br>Netherlands<br>United Kingdom and Ireland |
| 2. | Inventories in the context of the historical cost system | July 1974 (issued) | July 1975 (approved) | Canada<br>Japan<br>Mexico |
| 3. | Consolidated financial statements | November 1974 (issued) | October 1975 (approved after September 1975) | Australia<br>Germany, Federal Republic of<br>United States |
| 4. | Depreciation | April 1975 (issued) | July 1976 (approved after September 1975) | Australia<br>Canada<br>France |
| 5. | Information to be disclosed in financial statements | April 1975 (issued) | July 1976 (approved after September 1975) | Germany, Federal Republic of<br>Mexico<br>United Kingdom and Ireland |
| 6. | Inflation accounting | October 1975 | March 1977 | Canada<br>Israel<br>Netherlands<br>United Kingdom and Ireland |
| 7. | Translation of foreign accounts | March 1976 | July 1977 | Japan<br>Netherlands<br>United States |
| 8. | Source and application of funds | March 1976 | July 1977 | Australia<br>France<br>South Africa |

| | | Expected date of approval for publication: Exposure draft | Expected date of approval for publication: Definitive standard | Steering Committee members |
|---|---|---|---|---|
| 9. | Presentation of the income statement | July 1976 | November 1977 | Germany, Federal Republic of<br>Japan<br>United States |
| 10. | Research and development | November 1976 | March 1978 | Canada<br>Mexico<br>New Zealand |
| 11. | Events occurring after the balance sheet date and accounting for contingencies | March 1977 | July 1978 | Belgium<br>Japan<br>United Kingdom and Ireland |
| 12. | Accounting for certain types of long-term contracts | July 1977 | November 1978 | France<br>India<br>Mexico |
| 13. | Accounting for taxation in financial statements | November 1977 | March 1979 | Australia<br>Netherlands<br>United States |

a/ The membership of the International Accounting Standards Committee as of July 1976 is as follows:

Founder members

| | |
|---|---|
| Australia | The Institute of Chartered Accountants in Australia<br>Australian Society of Accountants |
| Canada | The Canadian Institute of Chartered Accountants in conjunction with the General Accountants' Association and The Society of Industrial Accountants in Canada |
| France | Ordre des Experts Comptables et des Comptables Agréés |
| Germany, Federal Republic of | Institut der Wirtschaftsprüfer in Deutschland e.V.<br>Wirtschaftsprüferkammer |
| Japan | The Japanese Institute of Certified Public Accountants |
| Mexico | Instituto Mexicano de Contadores Públicos, A.C. |
| Netherlands | Nederlands Instituut van Registeraccountants |

(foot-note continued on following page)

(Foot-note a/ continued)

| | |
|---|---|
| United Kingdom and Ireland | The Institute of Chartered Accountants in England and Wales<br>The Institute of Chartered Accountants of Scotland<br>The Institute of Chartered Accountants in Ireland<br>The Association of Certified Accountants<br>The Institute of Cost and Management Accountants<br>The Chartered Institute of Public Finance and Accountancy |
| United States | American Institute of Certified Public Accountants |
| Associate members | |
| Bangladesh | The Institute of Chartered Accountants of Bangladesh |
| Belgium | Collège National des Experts Comptables de Belgique<br>Institut des Reviseurs d'Entreprises<br>Institut Belge des Reviseurs de Banques |
| Denmark | Foreningen Af Statsautoriserede Revisorer |
| Fiji | The Fiji Institute of Accountants |
| Ghana | The Institute of Chartered Accountants (Ghana) |
| Greece | Institute of Certified Public Accountants of Greece |
| Hong Kong | Hong Kong Society of Accountants |
| India | The Institute of Chartered Accountants of India<br>The Institute of Cost and Works Accountants of India |
| Israel | The Institute of Certified Public Accountants in Israel |
| Jamaica | The Institute of Chartered Accountants of Jamaica |
| Korea | Korean Institute of Certified Public Accountants |
| Luxembourg | Ordre des Experts Comptables Luxembourgeois |
| Malaysia | The Malaysian Association of Certified Public Accountants |
| Malta | The Malta Institute of Accountants |
| New Zealand | New Zealand Society of Accountants |
| Nigeria | The Institute of Chartered Accountants of Nigeria |
| Pakistan | Pakistan Institute of Industrial Accountants<br>The Institute of Chartered Accountants of Pakistan |
| Philippines | Philippine Institute of Certified Public Accountants |
| Rhodesia | The Rhodesia Society of Chartered Accountants |
| Sierra Leone | The Association of Accountants in Sierra Leone |
| Singapore | Singapore Society of Accountants |

(foot-note continued on following page)

(Foot-note a/ continued)

| | |
|---|---|
| South Africa | The National Council of Chartered Accountants (SA) |
| Sri Lanka | The Institute of Chartered Accountants of Sri Lanka |
| Trinidad and Tobago | The Institute of Chartered Accountants of Trinidad and Tobago |
| Yugoslavia | Yugoslav Association of Accountant and Financial Experts<br>Social Accounting Service of Yugoslavia |
| Zambia | Zambia Association of Accountants |

b/ As of September 1975. Accounting for diversified operations and accounting for leases have been added to the Agenda in July 1976.

## Annex VII

### INTERNATIONAL ACCOUNTING STANDARDS COMMITTEE: DISCLOSURE OF ACCOUNTING POLICIES

(International Accounting Standard I - IAS 1)

International Accounting Standard I comprises paragraphs 16 to 23 of the statement issued by the International Accounting Standards Committee. The Standard should be read in the context of paragraphs 1 to 15 of this statement and of the Preface to Statements of International Accounting Standards.

"16. Going concern, consistency, and accrual are fundamental accounting assumptions. Where fundamental accounting assumptions are followed in financial statements, disclosure of such assumptions is not required. If a fundamental accounting assumption is not followed, that fact should be disclosed together with the reasons.

"17. Prudence, substance over form, and materiality should govern the selection and application of accounting policies.

"18. Financial statements should include clear and concise disclosure of all significant accounting policies which have been used.

"19. The disclosure of the significant accounting policies used should be an integral part of the financial statements. The policies should normally be disclosed in one place.

"20. Wrong or inappropriate treatment of items in balance sheets, income statements or profit and loss accounts, or other statements is not rectified either by disclosure of accounting policies used or by notes or explanatory material.

"21. Financial statements should show corresponding figures for the preceding period.

"22. A change in an accounting policy that has a material effect in the current period or may have a material effect in subsequent periods should be disclosed together with the reasons. The effect of the change should, if material, be disclosed and quantified.

"23. This International Accounting Standard becomes operative for financial statements covering periods beginning on or after 1 January 1975."

## Annex VIII

### INTERNATIONAL ACCOUNTING STANDARDS COMMITTEE: EXCERPTS FROM PARAGRAPH 13 OF THE STATEMENT OF INTERNATIONAL ACCOUNTING STANDARD I

"... The following are examples of areas in which differing accounting policies exist and which therefore require disclosure of the treatment selected:

"General

Consolidation policy

Conversion or translation of foreign currencies including the disposition of exchange gains and losses

Over-all valuation policy (e.g. historical cost, general purchasing power, replacement value)

Events subsequent to the balance-sheet date

Leases, hire purchase, or instalment transactions and related interest

Taxes

Long-term contracts

Franchises

"Assets

Receivables

Inventories (stock and work in progress) and related cost of goods sold

Depreciable assets and depreciation

Growing crops

Land held for development and related development costs

Investments: subsidiary companies, associated companies, and other investments

Research and development

Patents and trademarks

Goodwill

"<u>Liabilities and provisions</u>

Warranties

Commitments and contingencies

Pension costs and retirement plans

Severance and redundancy payments

"<u>Profits and losses</u>

Methods of revenue recognition

Maintenance, repairs, and improvements

Gains and losses on disposals of property

Reserve accounting, statutory or otherwise, including direct charges and credits to surplus accounts."

## Annex IX

## INTERNATIONAL ACCOUNTING STANDARDS COMMITTEE: INFORMATION TO BE DISCLOSED IN FINANCIAL STATEMENTS

(Excerpts from Exposure Draft 5, issued April 1975)

"8. The name of the enterprise, the country of incorporation, the balance sheet date, the period covered by the financial statements, and the currency in terms of which the financial statements are expressed should be stated. A brief description of the nature of the activities of the enterprise should be given if it is not otherwise apparent.

...

"11. Financial statements should show corresponding figures for the preceding period.

"12. Material events that have occurred subsequent to the balance sheet date but before the date on which the financial statements are approved for issue should be disclosed.

### Specific disclosures

"13. The specific disclosures set out in paragraphs 14 to 27 are based on the significant items affecting the financial statements of most industrial and commercial enterprises. Other types of enterprises, such as financial and insurance companies, should disclose information concerning the significant items affecting their financial statements.

### Balance sheet

#### General

"14. The following disclosures should be made:

(a) Restrictions on the title to assets

(b) Security given in respect of liabilities, stating whether the liability is secured on the assets of the enterprise or by the guarantee or assets of a third party

(c) Contingent assets and contingent liabilities, quantified if possible

(d) Contracts for future capital expenditure.

"15. Balance sheet items should not be offset against one another unless a legal right of offset exists.

"16. The methods of providing for pension and retirement plans for employees should be stated together with information as to how the liabilities arising are provided for.

Long-term assets

"17. Property, plant, and equipment. The following items should be disclosed separately, if material:

(a) Land

(b) Buildings

"18. If the title to property, plant, and equipment is not freehold or absolute, such assets should be included as separate items with an indication of the nature of the restrictions, for example, leaseholds or assets bought on hire purchase.

"19. The following amounts should be stated in respect of property, plant, and equipment:

(a) Acquisitions during the period

(b) Disposals during the period

(c) Accumulated depreciation at the end of the period.

Comparative amounts for the previous period need not be stated.

"20. If material, the net amounts of property, plant, and equipment held but not in use should be disclosed.

"21. Other long-term assets. The following items should be disclosed separately, if material, including, if applicable, the method and period of amortisation and any unusual write-offs during the period:

(a) Long-term investments

Investments in subsidiaries as defined in Exposure Draft 3 1/

Investments in associated companies as defined in Expcsure Draft 3 1/

Other investments

"1/ The number of the definitive International Accounting Standard will be shown when issued.

(b) Long-term intercompany 2/ receivables

(c) Other long-term receivables

(d) Goodwill

(e) Patents, trademarks, and similar assets

(f) Expenditures carried forward, for example, research and development, preliminary expenses, reorganization expenses, and deferred taxes.

Current assets

"22. The following items should be disclosed separately, if material:

(a) Cash

Cash includes cash on hand and current accounts and short-term deposits with banks. Cash which is not immediately available for use, for example, balances frozen in foreign banks by exchange restrictions, should be disclosed.

(b) Marketable securities, other than long-term investments

The market value should be disclosed if different from the carrying amount in the financial statements.

(c) Receivables

Accounts and notes receivable-trade

Receivables from directors and officers

Intercompany receivables

Other receivables

(d) Prepaid expenses

(e) Inventories.

---

"2/ The term "intercompany" used in this Statement refers to the presentation in the financial statements of balances or transactions between:

(a) A parent company and its subsidiaries

(b) A subsidiary and its parent company or other subsidiaries in the group

(c) A company and its associated companies."

## Long-term liabilities

"23. The following items, if material, should be disclosed separately, identifying the portion repayable within one year:

(a) Secured loans

(b) Unsecured loans

(c) Intercompany loans.

In respect to (a) and (b) the interest rates, repayment terms, conversion features, and the amounts of unamortized premium or discount should be shown.

## Current liabilities

"24. The following items should be disclosed separately, if material:

(a) Bank loans and overdrafts

(b) Current portions of long-term liabilities

(c) Payables

Accounts and notes payable-trade
Payables to directors and officers
Intercompany payables
Taxes on income
Dividends payable
Other accounts payable and accrued expenses.

## Other liabilities and provisions

"25. The following items should be separately disclosed, if material:

(a) Deferred taxes

(b) Deferred income

(c) Provision for warranties.

## Shareholders' equity

"26. The following disclosures should be made separately, if applicable:

(a) Share capital

For each class of share capital:

The amount of shares authorized and the amount issued and outstanding 3/

The capital not yet paid in

The par or legal value per share

The movement in share capital accounts during the period

The rights, preferences, and restrictions with respect to the distribution of dividends and to the repayment of capital

Cumulative preferred dividends in arrears

Reacquired shares

Shares under option including the terms and amounts

(b) Other equity, indicating the movements for the period

Capital paid-in in excess of par value (share premium)

Revaluation surplus

Reserves, indicating the restrictions, if any, on distribution

Retained earnings.

Income statement

"27. The income statement should give a clear understanding of the results of operations of the enterprise for the period. Pending the issue of further International Accounting Standards dealing with the income statement, at least the following information should be disclosed regardless of the format that is used:

(a) Sales or other operating revenues

(b) Depreciation

(c) Interest income and expense

(d) Income from investments

(e) Taxes on income

(f) Unusual charges or credits

(g) Significant intercompany transactions

(h) Net income.

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"3/ Shares outstanding refers to shares other than those held as 'treasury stock'. Treasury stock are a company's shares which it has reacquired and are legally available for reissue. This practice is not permitted in some countries."

## Effective date

"28. This International Accounting Standard becomes operative for financial statements covering periods beginning on or after 1 January 1977. (Note: this date is provisional.)"

# 3. SOME ASPECTS OF CORPORATE ACCOUNTING AND REPORTING OF SPECIAL INTEREST TO DEVELOPING HOST COUNTRIES*

## INTRODUCTION

1. The focus of attention of documents E/C.10/AC.1/2 and 3 has been on corporate accounting and reporting requirements from the standpoint of the international community as a whole. While the interests of shareholders and creditors, traditionally emphasized in corporate reporting, have continued to be regarded as an essential part of the whole, the multifarious concerns of public interest groups and of home and host Governments have also been highlighted. The standardization of accounting practices and the disclosure of additional information by transnational corporations for the enterprise as a whole within this broad framework would undoubtedly improve the usefulness of such information to developing host countries. Examples of such information are data on geographical spread, on segmentation by lines of business and on the activities of the various units of a transnational corporation group.

2. It may be useful, however, to make explicit some of the implications and to consider possible further requirements. The purpose of the present paper is to clarify some of these points. In addition to general purpose financial statements and non-financial reporting, some of the special purpose reports to Governments which appear to be particularly significant will also be considered. 1/

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* Originally issued as document E/C.10/AC.1/4, dated 4 August 1976.

1/ See also tables 1 and 2 in the annex for a survey of accounting and reporting practices in selected developing countries.

## I. GENERAL PURPOSE FINANCIAL STATEMENTS

3. A basic requirement of a host developing country in its dealings with transnational corporations operating in its territory is knowledge of the over-all characteristics and performance of these corporations. This knowledge is a prerequisite for evaluating alternative investment proposals. It is also essential for monitoring the over-all operations of transnational corporations once they are established in the host country. The absence of internationally accepted standards of accounting and reporting hampers meaningful comparisons between the over-all characteristics of transnational corporations, especially those based in different home countries. Inadequate disclosure of information restricts the efficacy of screening and monitoring. As a result, the positive contributions of transnational corporations to the development process are inadequately substantiated and fears of possible harm remain undispelled.

4. Greater transparency and improved reporting by transnational corporations are therefore essential if an atmosphere of confidence is to be established. In this regard, the disclosure in general purpose financial statements of items such as those included in the possible minimum list to be reported by transnational corporations is of relevance to developing host countries. The list should also serve as a general guide to reports of subsidiaries and associated companies operating in these countries. For purposes of illustration, information on intercompany transactions, on foreign exchange operations and on contributions to income, employment and production are singled out below for further amplification and clarification.

### A. Intercompany transactions

5. Intercompany transactions frequently account for a substantial proportion of the total transactions of transnational corporations and their subsidiaries. These transactions, being transfers among units of the enterprise group, do not go through the usual market mechanism. Consequently, intracorporate transfer pricing may not correspond to prevailing prices in the market. While overinvoicing or underinvoicing may occur in intercompany merchandise trade, these practices may also apply to charges for services and rentals and interest on intercompany loans.

#### Transfer pricing

6. The setting of suitable prices in intercompany transactions is inherently difficult, since an arm's length price can only be applied if identical goods and services are traded among unrelated entities. This is frequently not the case with respect to the kinds of products or services that account for a large part of intercompany transfers. A notable example of such a transfer is the shipment of intermediate products for further processing from headquarters to a foreign subsidiary. These products may be overcharged, for example to reduce taxes in the host country. Foreign exchange controls and other considerations may also influence pricing practices.

7. Although adequate scrutiny of transfer pricing requires the detailed examination of corporate records, usually by tax authorities, as in the experience of the United States where there are elaborate arm's length rules (e.g. section 482 of the United States Internal Revenue Code), the disclosure of a consistent set of principles governing transfer pricing in general purpose financial statements could go a long way towards restoring credibility. For instance, even if arm's length pricing was found impractical, the consistent application of approximations such as the cost plus method would demonstrate the absence of artificial manipulation and would facilitate spot checking by the host Government.

Intercompany charges and overhead

8. Management, technical and consultancy fees, royalties, rental charges for equipment and interest expenses on parent company loans, like the price of goods transferred among units of a transnational corporation, may also deviate from the arm's length rule. Since these fees and charges payable by a subsidiary are costs chargeable against its income for the purpose of taxation, the Government in the host country has an interest in ascertaining the basis on which the amounts charged were determined.

9. For instance, the intercompany lending rate may differ significantly from prevailing rates for similar loans in the country in which the lender is located. In some cases, capital expenditures by subsidiaries are financed by the parent company by means of loans at relatively high rates of interest rather than by an increase in the subsidiary's equity. This may be done to reduce the subsidiary's tax liability - interest being an expense chargeable to income for tax purposes while dividends are paid out of the subsidiary's post-tax income. Parent companies may also prefer loan financing in the case of subsidiaries located in host countries where the remittance of profits is restricted but debt service payments are freely transferable.

10. Though certain charges may sometimes be reported separately in the financial statements of subsidiaries, they are frequently combined with other, usually local, expenses and reported under the heading operating expenses or administrative expenses, as appropriate. Although tax authorities can, in principle, obtain the relevant information directly from the subsidiaries on a confidential basis, local shareholders and others wishing to appraise the subsidiaries' financial results must depend on whatever information is disclosed by them in the financial statements. The reporting of the amounts of these charges, while helpful, may not be sufficient to permit an evaluation of results: it may also be necessary for the subsidiary to disclose the method used in determining the amount charged to it.

11. With respect to overhead expenses, such as research and general administration, the question is largely not one of pricing but rather one involving the principle of allocation. Some knowledge of the enterprise as a whole is required to evaluate the fairness of the allocation. In addition to the disclosure of the principles on which the allocation is made, separate reporting in the financial statements of subsidiaries of the amount of such expenses related to the operations of the subsidiaries also appears to be desirable.

## B. Foreign exchange transactions

12. The capacity of foreign subsidiaries to earn or save foreign exchange is usually a major consideration of Governments in developing countries in granting various fiscal incentives and other privileges in order to encourage their establishment. In order to monitor the performance of subsidiaries in contributing to the host countries' foreign exchange resources, Governments need comprehensive and detailed information on their external transactions. While such information will be provided mostly in special purpose reports, general purpose financial statements should include at least some of the major items pertaining to these transactions. Such financial statements could include not only actual receipts and disbursements of foreign exchange but also changes in foreign assets and liabilities.

13. The items to be reported in this connexion might include the following:

(a) Exports of goods and services;

(b) Imports of goods and services (including fees and charges payable to the parent company);

(c) Interest payable on external loans;

(d) Interest receivable on external loans made by the subsidiary;

(e) Proceeds from external loans;

(f) Repayment of external loans;

(g) External loans extended by the subsidiary;

(h) Repayment received on external loans;

(i) New inward foreign direct investment;

(j) New outward foreign direct investment;

(k) Dividends payable abroad;

(l) Dividends receivable from abroad.

## C. Contribution to income, employment and production

14. Foreign exchange contributions are, of course, only one aspect of the over-all contribution, whether positive or negative, to the host country's economy. General purpose financial statements of the subsidiary could also include a value-added statement. Value added can, of course, be reflected in the difference between the value of the company's sales and that of its purchased inputs in the income statement. The amount thus calculated can then be analysed by application, namely

wage and salary payments, payments for the use of capital (interest and dividends), taxes payable to Government and provisions for the replacement and expansion of assets (depreciation and reinvestment of profits). If all these items are broken down by source and destination into domestic and foreign, the balance would provide an approximate measurement of the subsidiary's relative contribution to the local economy.

15. It should be noted that the value-added statement of a foreign subsidiary can be affected by transfer pricing practices involving overstatement or understatement.

## II. NON-FINANCIAL REPORTING

16. The information requirements of developing host countries are not limited to financial statements. Numerous non-financial items are of crucial importance in appraising the contribution made by transnational corporations to development.

### Employment and labour

17. Apart from its relevance to value added, information in the subsidiary's general purpose report on the size and patterns of employment is required to shed light on the subsidiary's use of local manpower and its employment and training policies. Some of the basic items in this area have been indicated in section E of the annex to document E/C.10/AC.1/2. These can easily be extended to include supplementary information on labour conditions, such as health and safety measures. The factual information can be accompanied by a review of the company's policies and plans which have a bearing on the future employment of various categories of labour.

### Production

18. No less important than the reporting of employment and labour is information on physical production, domestic and foreign sales, and the use of domestic materials in the production process. While such information is often furnished to one or more departments of the host country Government for the compilation of production statistics, and, at longer intervals, in connexion with industrial censuses or surveys, the inclusion of some basic quantitative production data in the general purpose annual reports of subsidiaries appears to be desirable. The information should shed light on intra-industry relations and on linkages between the foreign subsidiary and local producers of raw materials and manufacturing products.

19. The impact on environment could be considered as an aspect of production in a broad sense. Environmental improvements would constitute a social product while pollution would represent a negative product. Some items in this area have been indicated in section E of the annex to document E/C.10/AC.1/2.

## III. SPECIAL PURPOSE REPORTS TO GOVERNMENTS

20. Despite the importance attached to general purpose reports and possible ways of improving them, it is evident that much pertinent information can only be made available in special purpose reports to Governments. Whether with respect to foreign exchange transactions, labour conditions or environment, the information contained in general purpose reports of transnational corporations and their subsidiaries is necessarily limited, not only because of the cost of the general distribution of massive information but also by considerations of confidentiality. Considerations of cost and confidentiality apply equally to information for many other purposes, such as evaluation of the type of technology transferred and possible restrictive business practices.

### Information prior to entry

21. Most developing countries have established some machinery for the evaluation of foreign investment projects, and an increasing number of countries have set up special bodies, such as investment boards, which deal with all matters relating to foreign direct investment, including the screening and selection of projects, the granting of investment incentives, assistance with the registration of companies and other formalities connected with the establishment of a business and its start-up.

22. The submission of an investment proposal for government approval frequently involves the presentation of a detailed report on the nature of the proposed investment, the capitalization envisaged, the capacity to be installed, the manpower required, the nature of the products to be manufactured, the markets (domestic and foreign) to be served, the source and nature of the raw materials to be used, and so on. A detailed technical report may also be required, describing the equipment and technology to be employed, power and transportation requirements, and so forth.

23. In some countries, investment boards are also charged with monitoring the execution of the project and the observance of the terms of the investment law or agreement.

### Information on operations

24. Foreign subsidiaries, like domestic companies, are required to submit reports on various aspects of their operations to government agencies concerned with the compilation of economic, financial and social statistics. Most developing countries undertake periodic industrial censuses and an increasing number prepare and publish indices or data on the production of key commodities and manufactures.

25. The compilation of national balance-of-payments statistics also involves the annual submission of detailed information on the companies' external transactions. That information is treated as confidential and published only in aggregated form. Both industrial and balance-of-payments data are usually reported in accordance with the relevant international classification (ISIC for industrial data and for balance-of-payments statistics, the standard classification used by the members of the International Monetary Fund). Information

on employment and wages and on the observance of labour laws (including provisions concerning expatriate employment) is also required in many developing countries.

26. Government departments and agencies, notably the treasury and exchange control authorities, are usually empowered to demand the submission as required of supplementary, confidential information to permit an appraisal of the operations of foreign subsidiaries in the areas concerned. For instance, if artificial transfer pricing is under investigation, pertinent information may be required to be submitted to the treasury. Such information can be voluminous. Similarly, if evasion of foreign exchange control regulations or violations of anti-trust or environmental protection provisions are in question, the information called for can also be massive.

27. Thus, there are practical administrative difficulties in handling and interpreting the data. In some cases, the authorities can be embarrassed by too much, rather than too little, information, because not all the available information is relevant and the meaning of particular pieces of information is not always clear. On the other hand, key pieces of information, such as tax returns in the home country, may not be available.

28. It has been generally recognized that information on the operations of transnational corporations is an essential tool for developing host countries in their dealings with these corporations. It is therefore important that the Governments of these countries should be provided with the information necessary for the proper appraisal of the activities of transnational corporations and their subsidiaries. The usefulness of the information depends, however, on the capacity of the Governments to evaluate and interpret it. International standardization of accounting and reporting can strengthen this capacity but it can not take the place of adequate administrative machinery and expertise in the developing host countries in their dealings with transnational corporations.

Table 1. Selected developing countries: reporting and disclosure requirements and practices

| Country | Certified financial statements filed annually: By all companies | Certified financial statements filed annually: By specified companies (regulated, publicly traded, over certain size) | Statutory financial statements prepared in accordance with official format | Statement of changes in financial position included in general purpose financial statements | Accounting practices adhere strictly to tax requirements | Accounting principles chosen to meet given circumstances disclosed | Basis on which fixed assets are stated is disclosed | Method of computing depreciation disclosed | Inventory carrying basis disclosed | Basis of foreign currency translation disclosed |
|---|---|---|---|---|---|---|---|---|---|---|
| Argentina......... | R | R | R | MI | MI | MA | R | R | R | R |
| Bolivia.......... | N | R | N | MI | MA | MI | MA | MI | H | MI |
| Brazil........... | N | R | R | MI | MA | H | R | MI | MA | MI |
| Chile............ | N | MI | R | MI | MI | H | MA | MI | MI | MA |
| Colombia......... | N | R | R | MI | H | MI | MI | MI | MI | MI |
| Ethiopia......... | N | R | N | MI | MI | MI | MA | MI | MA | MA |
| India............ | R | R | R | MI | N | MI | R | MI | N | MI |
| Iran............. | R | R | ... | MI | MA | MA | MA | MA | MA | MA |
| Kenya............ | R | R | N | N | N | H | R | H | H | R |
| Malaysia......... | R | R | N | MI | N | N | R | MI | MI | R |
| Mexico........... | N | R | N | R | MI | R | R | R | R | R |
| Nigeria.......... | R | R | N | MI | N | MI | R | MI | N | R |
| Pakistan......... | N | R | R | MI | N | N | R | H | MI | R |
| Peru............. | N | R | R | R | H | R | R | R | R | R |
| Philippines...... | R | R | R | H | N | R | R | R | R | R |
| Singapore........ | R | R | N | MI | N | R | R | R | MI | R |
| Venezuela........ | R | R | R | R | NP | R | R | R | R | R |
| Zaire............ | N | R | N | N | N | N | MI | MI | MI | N |

Source: United Nations Centre on Transnational Corporations, based on A Survey in 46 Countries: Accounting Principles and Reporting Practices, Price Waterhouse International, 1975.

Key:

| | | | |
|---|---|---|---|
| R | Required by law or otherwise mandatory | MI | Practice of minority of companies |
| MA | Practice of majority of companies | N | Not found in practice or not applicable |
| H | Practice of about half of companies | NP | Not permitted |
| | | ... | Information not available |

Table 2. Selected developing countries: reporting requirements and practices with respect to selected items of financial information

| Country | Historical cost statements accompanied by statement or note showing effects of price level changes | Intercompany receivables shown separately | Intercompany payables shown separately | Long-term debt: amount outstanding, terms, interest rate disclosed | Sales and other revenue in reporting period disclosed | Cost of sales disclosed | Sales for each class of business disclosed |
|---|---|---|---|---|---|---|---|
| Argentina........ | MI | P | R | MI | R | R | N |
| Bolivia.......... | N | MI | MI | MI | MA | MA | MI |
| Brazil........... | MA | R | R | MI | H | MI | MI |
| Chile............ | a/ | H | MI | H | R | R | N |
| Colombia......... | N | MI | MI | MI | MA | MA | MI |
| Ethiopia......... | N | MA | MA | MA | MA | MA | MI |
| India............ | N | R | MI | MA | R | MA | R |
| Iran............. | MA | MA | MA | MA | MA | MA | MA |
| Kenya............ | MI | MA | R | H | H | MI | MI |
| Malaysia......... | N | R | R | MA | MI | MI | MI |
| Mexico........... | N | R | R | R | R | R | MI |
| Nigeria.......... | N | R | R | MA | MI | MI | MI |
| Pakistan......... | N | MA | MI | MA | R | H | MI |
| Peru............. | N | R | R | MI | R | R | N |
| Philippines...... | MI | R | R | MA | R | R | MI |
| Singapore........ | N | R | R | MA | MI | MI | MI |
| Venezuela........ | N | MA | R | R | R | R | MI |
| Zaire............ | N | MI | MI | MI | MA | H | N |

Source: See table 1.

Key: See table 1.

a/ Historical cost financial statements replaced by price-level adjusted statement.

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