

ROMANIAN ACCOUNTING AND AUDIT REFORM IN THE WAY OF ACCESSION INTO THE EUROPEAN UNION

Adriana Tiron Tudor

Economic Faculty, Babes Bolyai University, Cluj Napoca, Romania

Abstract: *The aim of the research is to establish the specific phases of the Romanian accounting and auditing regulations harmonization with aquis communautaire with them inherent problems.*

The first section sets out some of the main steps of global convergence activities and related research as well as the recent regulatory developments following the convergence attempts to the global set of financial accounting standards. A separate section is dedicated to a brief history of accounting and the current accounting system in Romania. In this section we emphasize variations from and similarities with the IFRS/IAS. The paper concludes with a discussion of the effects of convergence on the financial reporting and accounting systems in Romanian and the expectations of the users of financial information.

The research was carried out on the basis of the available sources (more of them are electronic sources, via internet) and research methods like historical analyses, comparisons. We conduct also an empirical research based on questionnaires and interviews with chefs of accounting departments from companies with different size and type of business, publicly traded. A very important role in writing the papers played our experience in IAS implementing procedures, based on our experience like practitioners.

Key words: implementing IAS/IFRS, national standards, Romanian experience

1 Introduction

In the last period of time, the globalization process evolution was accelerated. Globalization of capital markets and the expansion of investment and financing activities require a common language for business environment. Regarding the financial information, the basic elements of a common language are a single global accounting, reporting and disclosure set of standard.

International Financial Reporting Standards being focused on the capital market financial information needs makes significant progress toward global recognition. On this way European Commission adopts IFRS for listed companies beginning January 2005. For the applicant countries this means a separate market driven convergence for listed companies in addition to the bureaucratically driven convergence of accession assessment¹.

In the late last century², Romania, like other transitional economies from the central and East Europe region, seeks to adapt to, or join, the international community.

In this way, there have been moves to adopt international accounting and reporting standards (IAS/IFRS) and the European Directives (UE rules) either for a part or all of the country's private enterprises.

¹ Day, J., Taylor, P. – Accession to the European Union and the Process of Accounting and Audit Reform, Journal Accounting in Europe, vol2, 2005 pag . 10

² Tiron, T. A., Mutiu, I. A. - Problems faced and solution developed during the implementation of IAS/IFRS – romanian experience, 1st International Accounting Conference: On the way to Convergency, Accounting Academicians' Collaboration Foundation, 2004, Istanbul, Turquie , pag. 2

The aim of the research is to establish how the specific phases of the accounting regulations harmonization affected Romanian accounting and accountants.

The paper is organized as follow. The next section sets out some of the main steps of global convergence activities and related research as well as the recent regulatory developments following the convergence attempts to the global set of financial accounting standards. A separate section is dedicated to a brief history of accounting and the current accounting system in Romania. In this section we emphasize variations from and similarities with the IFRS/IAS. The paper concludes with a discussion of the effects of convergence on the financial reporting and accounting systems of domestic, multinational enterprises, and audit firms in Romania, and the expectations of the users of financial information.

The research was carried out on the basis of the available sources (more of them are electronic sources, via internet) and research methods like historical analyses, comparisons. We conduct also an empirical research based on questionnaires and interviews with chefs of accounting departments from companies with different size and type of business, publicly traded. A very important role in writing the papers played our experience in IAS implementing procedures, based on our experience like practitioners.

2 Convergence activities

2.1 The global trend

Currently³, the global trend is convergence of accounting standards in which the ultimate goal is to create a single set of high quality standards.

The process of international accounting harmonization was initiated as a result of the globalization of the financial markets in order to respond to the compatibility and comparability requirements concerning the listed companies' financial statements.

The benefits for business and for national governments of adopting IAS/IFRS are a relevant, high quality, comparable reporting, which encourages cross-border investment. Transparent reporting will lower the cost of capital - both for companies and for the country itself. And it will help create the conditions for market stability and economic growth.

In the last two decades, International Accounting Standards Committee (IASC) issued International Accounting Standards (IAS) and International Financial Reporting Standards with which national bodies tried to harmonize their own rules. IASC have a greater national and regional support.

There is a rich related literature with studies pro or contra accounting convergence. Like example, the "pro group" state that the main benefit is the elimination of arbitrary assumptions to set financial statements to the same base while arguing harmonization may not be essential for security investors since they use decision criteria independent of accounting manipulations (Goeltz, 1996). The "contra group" argument against harmonization is related to the 'accounting colonialism' imposed on developing countries by the developed countries (Chandler, 1992).

A recent study about adopting IFRS, shows that several nations have already taken steps to converge their regulatory framework with the requirements of the International Financial Reporting Standards (IFRS/IAS) (Street, 2003a).

Thus, the GAAP Convergence 2002 survey carried out by the six largest accounting firms in the world⁴, shows that 95% of the 59 surveyed countries either have adopted, intend to

³ Can Simga-Mugan, Nazli Hosal-Akman -Convergence to international financial reporting standards: the case of Turkey ,Int. J. Accounting, Auditing and Performance Evaluation, Vol. 2, Nos. 1/2, 2005 pag. 127.

adopt or intend to converge with IFRS, considering IASB the appropriate body to develop a global accounting language. But the same survey identifies some of the significant obstacles to achieving convergence, such as:

- Disagreements with the requirements of certain significant IFRS - for example, financial instruments and other standard based on fair value accounting (39% of the cases);
- Tax-driven nature of the national accounting regime and the tension wield on the capital markets and companies, which desire to adopt IFRS (47%);
- Complicated nature of particular standards may have as a result the limited implementation of IFRS to listed companies, widening the gap between IFRS and the national accounting standards used by small and medium-sized entities –SMEs – (51%);
- Insufficient guidance on first-time application of IFRS (35%);
- Limited capital markets (30%);
- Satisfaction with national accounting standards among investors/users (21%);
- Translation difficulties (18%).

Related to Romania, we can say that Romania is confronted with all this obstacles in achieving convergence.

In the majority of the cases, only the listed companies will have to adopt IFRS while, in other countries, national accounting standard setter will try to remove the differences between IFRS and national standards, covering listed and unlisted companies. Thus, 60% of the surveyed countries intend to replace their national regulations with IFRS for listed companies, supplemented only for national issues not addressed in IFRS.

Also, 72% of the surveyed countries have a formal policy to adopt or converge with IFRS (of the 39 of these countries, 25 are EU Member States or states that plan to join the European Union). The intention to converge can take either the form of a governmental requirement (in 57% of the cases) or a policy announced by the national accounting standard setting body.

2.2 *European environment*

The European Commission's recommendation that all listed companies in the European Union should, by 2005, prepare their consolidated financial statements using IAS/IFRS is the most significant change to European financial reporting since the Accounting Directives of the 1970s - and a clear signpost for those countries which, like Romania, are looking towards entry to the Union. Although Romania is not in the "first wave" of enlargement countries, it can expect to find that by the time accession is being negotiated; all public companies and many others in the EU will be using IAS.

At the beginning of year 2004, Sir David Tweedie⁵ talked about the convergence process in these words: "European Union gave us a lot of credibility [...]. By 2005, 91 countries will either allow or require IAS's. However, EU adoption means that companies have to be able to start applying IAS's at the start of the fiscal year 2004, so that they have comparable results for the 2005 adoption deadline"⁶.

However, the year 2005 proved itself to be more difficult than expected since more issues emerged. A particular attention was given (and it is still) to the sensitive balance between

⁴ BDO, Deloitte Touche Tohmatsu, Ernst&Young, Grant Thornton, KPMG, PricewaterhouseCoopers, GAAP CONVERGENCE 2002- A Survey of National Efforts to Promote and Achieve Convergence with IFRS

⁵ president of UK-ASB, subsequently elected president of IASB

⁶ Tweedie speaks out, Accountancy, January 2004, pag.56-58

consistency and flexibility of the accounting regulations and practices across Europe. Also, a fervent debate was caused by the certain users and countries request for an additional layer of interpretations of the IFRS.

2.3 *The role of aquis communautaire*

The primary references about accounting and audit requirements for public and private companies are found in the Fourth and Seventh Directives on Company Law which prescribes accounting recommendation and in the Eighth Directive which relates to auditing.

The compliance with aquis communautaire in the field of accounting and audit is a requirement for candidate states but not a compulsory condition, so we can say that accounting and auditing issues have a subsidiary role in accession assessment. Analyzing the full compliance with the aquis in the existing members states “we may also find articles that have not been properly implemented⁷”.

The Fourth and Seventh Directives passed a process of harmonization with International Accounting Standards responding in this way to the capital market information needs.

2.4 *The role of International Financial Reporting and Accounting Standards (IFRS/IAS) in Central and Eastern Europe*

As transitional economies seek to adapt to or join the international community there have been moves to adopt or adapt international accounting standards (IAS) and international audit standards either for a part or all of the country's enterprises.

Beginning in 2005, the European Union (EU) will require all EU listed companies to produce consolidated financial statements in accordance with International Financial Reporting Standards (IFRS/IAS). This presents a real challenge to listed companies in both current EU member states and candidate countries, since at present a wide range of accounting standards are employed across Europe.

Studying⁸ the accounting requirements for listed companies in 2003 in nine Central and Eastern European (CEE) countries: Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia Croatia and Romania the conclusion is that in each country, the accounting standards are determined by the listing rules of the respective stock exchange. Seven of the nine stock exchanges in question (Bratislava, Budapest, Ljubljana, Prague, Riga, Tallinn, Vilnius, Warsaw and Bucharest) have more than one market segment; the Tallinn Stock Exchange has only one market segment.

Implementation of IAS in these nine markets may be summarized as follows:

- IAS-compliant financial statements are obligatory for listed companies in the main market in five countries: Czech Republic, Estonia, Latvia, Lithuania and Slovakia.
- In Hungary, companies may produce financial statements according to national law, IAS or US GAAP.
- In Poland, the home country of the issuer determines whether Polish Accounting Standards, IAS or US GAAP may be applied.
- In Slovenia and Romania companies produce financial statements according to National Accounting Rules, which at present are not completely IAS-compliant.

⁷ Day, J., Taylor, P. – Accession to the European Union and the Process of Accounting and Audit Reform, Journal Accounting in Europe, vol2, 2005 pag . 9

⁸ Tiron, T. A., Mutiu IA - Problems faced and solution developed during the implementation of IAS/IFRS – romanian experience, 1st International Accounting Conference: On the way to Convergency, Accounting Academicians' Collaboration Foundation, 2004, Istanbul, Turquie , pag. 4

In 2005 we analysed the direct use of IFRSs in some countries from East Europe. By direct use we understand that the basis of preparation note and the auditor's report will refer to conformity with IFRSs. The results are synthesized like follows:

- IFRSs are required for All Domestic Listed Companies Bulgaria, Croatia, Macedonia and in Bosnia and Herzegovina for all large and medium sized.
- In Bulgaria the Accountancy Act provides the legal framework of accounting. The Law require the application of the IFRS adopted by the European Union Committee on the territory of Bulgaria.
- IFRS are not permitted for domestic listed companies in Moldova.
- There isn't a domestic stock exchange in Albania so companies (unlisted) follow Albanian GAAP.
- IFRSs are required for some domestic listed companies in Romania, companies of national Importance.
- IFRSs are required for all domestic listed companies in Czech Republic, Hungary, Poland, Slovenia and Slovak. For these countries the audit report and basis of presentation note will refer to compliance with "IFRSs as adopted by the EU". Currently, the EU has adopted all IFRSs, though one aspect of IAS 39 was modified. The modification affects only a tiny percentage of EU companies following IFRSs. Also, EU and EEA member states are permitted to defer the application of IFRSs until 2007 (a) for companies that only have debt securities listed in a public securities market and/or (b) for companies whose securities are admitted to public trading in a non-member state and that, for that purpose, have been using internationally accepted standards other than IFRSs (such as US GAAP) since a financial year that started prior to adoption of the European IAS regulation.

3 The harmonization process of Romanian Accounting and Audit System with European and International Standards – an overview

3.1 Ex Romanian accounting system

The implications for Romania, and other emerging markets, are clear. The general consensus of expert opinion is that a country's prospects of economic success are enhanced if it adopts internationally recognized standards in each of these areas.

The Romanian financial reporting and auditing requirements⁹ are continuing to undergo change and progression to move toward application of standards comparable with the European Union. From when market economy changes began in the 1990, it has taken some time for financial reporting in Romania to develop, as for much of the past period it has been directed to the provision of information to the State authorities and has not had as a major focus the provision of information to investors (current and prospective owners), management, financial institutions and other common users of financial reports in an international context. Financial reporting (and accounting in general) in Romania has tended to be more about "form" than about "substance", that is following the steps, having a relevant piece of paper, dotting the "I's" and crossing the "T's", rather than focusing on whether the figures presented reflect the actual financial position of the reporting entity at the period end and the results from activities during the period being reported on.

Before proceeding to detail the stages of harmonization process, we consider absolutely necessary to present the main characteristics of the ex Romanian accounting system. Through them, the understanding of the changes made became more obviously.

⁹ www.ey.com- Financial reporting in Romania

Accounting in Romania is regulated by the provisions of Law 82/1991 (the Accounting Law), republished January 2005.

In 1994 a system of accounting, based on the French system and incorporating a revised "chart of accounts" was introduced. The Romanian accounting system were codified and rule driven, being based to a large extent on the French model, with a chart of accounts consisting of some 100 obligatory accounts, each with its account name and number defined by law.

For each new activity (see the case of leasing, merger, provisions) the Ministry of Public Finances issued a methodological guideline, with accounts, accounts correspondence and registration flows, obligatory to follow.

The Accounting system Romania adopted in 1994 can be generally described as a system designated to inform the main user groups. Historically, accounting in Romania was directed towards providing information to two user groups: the Tax Authorities and the Government. This led to the financial statements that were being prepared according to regulations that allowed very little scope for judgmental accounting entries, provided limited disclosure, and as a result were of very limited use to other users (shareholders and management).

Another characteristic of the ex accounting system is the strong connection between taxation and accounting. While the system allowed for a degree of judgment in recording accounting entries, in practice those which did not have any tax consequences were rarely made, reflecting the unwillingness of most accountants to record entries other than those that we required to calculate taxable profit.

Concerning the structure of profit and loss account, it should be noted that Romanian expense accounts were categorized by nature rather than destination, thus these included accounts such as "Wages and Salaries", "Depreciation of Fixed Assets", etc., rather than cost of sales, marketing costs, etc. However, with a reasonably good, preferably data based driven accounting system, it is not too difficult to meet both Romanian statutory reporting needs and management and group reporting requirements.

Although the standard chart of accounts included a couple of dozen of provision accounts, it is very unusual to see any of these used.

According to the law, the financial year started on January 1 and concludes on December 31, with the exception of the first year of activity when it begins on the date of formation.

All Romanian companies had to have a December 31 year-end. Supposed a Romanian company is a subsidiary of an international companies group that has a different year-end, the Romanian company must prepare two separate closures.

3.2 Current Romanian accounting system

As a result of the continued need for increasing transparency, improving Corporate Governance and compliance with European Union Directives, the harmonisation process had started (financed by the UK Government). The process aim was to amend again the accounting regulations so that they should be better complied with International Accounting Standards (IAS) issued by International Accounting Standard Committee (IASC) and with the requirements of the EU IV-th Directive.

In Romania within the framework of the Accounting Development Program it was been developing the Romanian Accounting System (RAS). The old system provided information principally for Government tax and statistical purposes. The new RAS provides the type of information needed by investors, both domestic and international, and other users of accounts

such as lenders, employees, suppliers, customers, etc., writes the «Strategy for Romanian Accountancy Development», a publication financed by the UK's DFID.

Fundamental changes to legislation have occurred including:

- harmonization of Romanian financial reporting with the requirements of International Accounting Standards and the European Union 4th Directive - Minister of Finance Order 94/2001 (MoF Order 94/2001)
- harmonization of the financial reporting for Romanian companies not applying MoF Order 94/2001 with the requirements of the European Union 4th Directive - Minister of Finance Order 306/2002 (MoF Order 306/2002); and
- the establishment of a body responsible for the training and regulation of the independent audit function in Romania, the Chamber of Auditors - Emergency Ordinance 75/1999 (EO 75/1999) as approved by Law 133/2002.

As a result of this process, IAS has effectively started to be rolled out in Romania, with 197 companies being required to apply IAS for the first time in respect of the year ended 31 December 2000.

MoF Order 94/2001 and subsequent regulations have imposed some non-compliance with International Financial Reporting Standards (IFRS), however at the same time there is an indication for firms that report under MoF Order 94/2001 that they are required to be fully compliant with all applicable International Financial Reporting Standards for the year ending 31 December 2006 reporting.

The practical application of the new accounting regulation, Orders of the Ministry of Finance (OMPF) - OMPF no.403/2000 (which was revoked shortly after issuance), started for a sample of companies. The new accounting system has been run with the oldest for the financial year ended 31 December 1999.

Over a maximum of ten years, companies will be brought within the improved regime according to their size. Listed companies will be among those entities in the first batch, as those are the entities most in need of financial statements that address user needs.

For this aim was issued the Order no. 94/2001 of the Ministry of Public Finances on accounting regulations harmonized with the 4th Directive of the European Communities and with the International Accounting Standards.

Under the terms of Order no. 94 of January 29, 2001, Romanian Accounting Law was harmonized with the IVth Directive of the European Union and with International Accounting Standards. All quoted companies, state corporations and all companies working in the capital markets had to apply the new Romanian Accounting Standards starting with the year 2000. These new rules (at that time) became progressively compulsory for other largish companies based on total assets, turnover and number of employees for the previous year, as follows:

<i>Year ending</i>	<i>Turnover (Million Euro)</i>	<i>Total assets (Million Euro)</i>	<i>Employees</i>
December 31, 2002	8	4.0	200
December 31, 2003	7	3.5	150
December 31, 2004	6	3.0	100
December 31, 2005	5	2.5	50

Companies who meet these criteria must be audited, under the provisions of the Government Emergency Ordinance no. 75 of 1999.

Smaller companies may choose to apply the new rules if they had obtained an approval from the Romanian Ministry of Finance.

Starting with the 2006 year-end, small and medium enterprises (as defined by the existing legislation at that time) only will be left outside the scope of the regulations. These enterprises will apply the provisions of the republished accounting law 82/1991 and the Regulations 306/2002, for the approval of Simplified Accounting Regulations harmonized with the European Directives, which is a simplified version of Order Nr 94 of January 29, 2001.

The introduction¹⁰ of MoF Order 94/2001 has seen an increase in the level of disclosure of information in notes and adding additional reporting requirements (including introduction of cash-flow statements and statements of changes in shareholders equity) and an increasing emphasis on provisioning and accruals considerations, although there is still, in some cases, an inclination to limit the differences between accounting and taxation profit.

In Ernest and Young company opinion, MoF Order 94/2001¹¹ introduced, among other items, the following issues for Romanian financial accounting and reporting:

- Application of indexation measures to reflect the impact of inflation (both in establishing opening values and on an ongoing basis) - in limited cases, and not for financial statements to be submitted to the Ministry of Finance (except for specific adjustments to fixed asset values in accordance with GD 403/2000 and subsequent regulations GD 1553/2003). Until 31 December 2003 such revaluations were considered to be tax deductible, for 31 December 2004 reporting, while revaluations can occur for financial reporting they will not be considered for tax purposes;
- Deferred taxation, to include the impact of differences between temporary taxable differences arising between accounting and fiscal taxation balance sheet values differing and from the impact of carried forward tax losses;
- Emphasis on substance rather than form;
- Disclosure of related party balances and transactions;
- Differences between accounting depreciation and taxation depreciation;
- Additional schedule disclosures, such as cash-flow statements and statements for change of shareholders' equity;
- Assessment of impairment of assets;
- Segment reporting;
- More detailed disclosure notes;
- More specific inventory cost valuation calculation;
- Financial instrument reporting.

About consolidated financial statements for a company and its subsidiaries, are currently not required by the legislation relating to completion of statutory financial statements for MoF Order 94/2001 compliant companies. Law 82/1991 (republished in January 2005) requires that the standards in the International Financial Reporting Standards relating to consolidation should be applied commencing with the year ending 31 December 2006.

There were a lot of problems and questions about implementing the new regulations, because IAS is the output of an accounting culture strongly anchored in principles and professional judgement. By asking the Romanian companies to prepare financial statements in accordance with Accounting law, OMPF 94/2001, but also with IAS and accounting framework, there can burst out a possible conflict. Even if at the European level it was

¹⁰ www.ey.com- Financial reporting in Romania

¹¹ www.ey.com- Financial reporting in Romania

decided that there are not significant differences between IAS and Directives, nationally these may appear. At least regarding the terminology used by IAS and by the European Directives there are differences related to each one's specific origin. For example, art.7 of OMPF 94/2001 states that in the situation of a conflict between these two, the companies have the possibility to choose to endorse the accounting treatment that ensures the fair view of the respective transaction. At a closer look, OMPF 94/2001 reveals strong influences of IASB, such as:

- The valuation of the research expenses – according to OMPF 94/2001 these will be recognized in the balance sheet only in certain situations described in volume III, this is a direct link to the old IAS 9 revoked in 1998;
- The case of the maximum period of amortization of the consolidated goodwill (20 years) – art.5.2.b OMPF 94/2001 – was part of IAS 22, also revoked and replaced with IFRS 3;
- From the nine principles in OMPF 94/2001, six have origin in the Fourth Directive and three in IAS1. Thus, the materiality principle is taken from IAS 1 and represents a new concept for Romania, while substance over form concept, even if in IAS 1 is a key element in determining the relevance of the financial statements, in OMPF it is just placed along with the other principles.

There were some problems about¹²:

- Limited inclusion of provisions for items of inventory that may be sold for less than the carrying value indicated or which may never be sold;
- No account is taken of the diminution in the purchasing power of the ROL. This means that non-monetary items (such as: property, plant and equipment (except where revalued), investments, inventory, share capital, individual income and expense items) do not reflect a "real" historical value;
- No separation between freehold and leased land and buildings is indicated;
- Disclosure of "related party" balances at the period end or transactions during the period although required for disclosure are in cases limited in what is included. In addition no consolidation concept exists where one entity has a majority ownership or control in/over another;
- Depreciation of fixed assets is based on historic ROL acquisition values (with in some cases Government specified revaluations of the ROL values having occurred) at State specified depreciation rates. In many countries tax and accounting rates differ, tax rates being specified, accounting being based on entity determined "useful life";
- Property, plant and equipment is recorded in ROL at the historic ROL value or based on State approved revaluation indices, neither of which results in an equivalent current ROL value for the acquisition cost. For 2000 onwards (under GD 403/2000, GD 1553/2003 etc.) valuations on a "fair value" base are allowed (and are tax deductible);
- Investments are included at historic ROL at the investment value and not at the equivalent current ROL value" at the acquisition/investment date;
- Foreign currency receivable or payables values are not adjusted by most entities until the end of the year. As a result, except for 31 December, for any other period end an accurate foreign currency receivable and payable balance is not indicated. Related to this, unrealized exchange gains and/or losses are only recorded at 31 December;
- Varying from entity to entity, limited use is made of accrual accounts to include all liabilities and expenses that relate to the activities undertaken in a specific period;
- No details of mortgages or security over assets given by the entity is indicated;

¹² www.ey.com- Financial reporting in Romania

- Reconciliation between different information within an enterprise both within the financial/accounting area and between this area and other areas or systems (such as production or sales) is not always performed on a regular basis or in a complete fashion or with differences being followed up and resolved. In many cases more than one system for collecting information by different parts of the entity may occur, with no centralized information being collected for use for different management decision-making, reporting or compliance purposes;
- Inventory valuation for manufactured goods tends to include an excessive amount of overhead compared to the recommendations of the applicable International Accounting Standard. Issues also arise in many entities on the basis used to arrive at standard costs and the means for allocating variances from standard. Inventory valuation is an area, where further development of accounting treatments followed, may be an issue;
- Due to diminution in the purchasing power of ROL, income and expense items from the prior year may not be useful for comparative purposes, unless restated into a historic "hard" currency value (such as US dollars) or indexed. For 2004 reporting this is less of an issue, with inflation decreasing and ROL maintaining its value against Euro and strengthening against the US dollar;
- No details on business relationships or remuneration of senior management is provided and/or no details of transactions with relations or related companies;
- No specific details on amounts due to the State and what is the split between principal and interest, and/or what amounts due may have been rescheduled. In the case of rescheduled amounts, there are no specific details on the terms for ongoing repayments. This area is beginning to improve with more detailed disclosures becoming more common.

In 2003 the Government by issuing OMPF 1827/2003 prolonged the terms of OMFP 94. Under OMFP 1827/2003 beginning with the 2005 financial statement, Romanian publicly traded companies are obliged by law to publish consolidated financial statements in conformity with IFRS adopted by the European Commission. But, till in March 2004, Romania doesn't had an official translation of IFRS in our national language, consolidated financial statements aren't used and the not application of IAS 29 regarding the inflation is recommended despite the real situation of our economy at that time. In article 6 of OMFP 1827/2003 is stipulated "Romanian companies presented inside the act will apply IFRS beginning with the 2005 financial statement". What are IFRS? They wrote: "International Financial Reporting standards, as presented and published by IASB". We have to underline at this time, Romania doesn't have an official translation of IFRS in our national language. So, this situation put the regular accountant in a delicate position. Let admit a person wanted to know more about IFRS. What does he had to do? The only solution was looking on Internet, because IFRS were not available anywhere in Romania. And there is another aspect: the practice in Romania is that every act issued by Ministry of Finance is followed by guideline rules, which tell the accountants exactly what they will do. Indeed, the guideline rules for Ordinance 1827 were not issued.

Ordinance no 1827 eliminate that inaccuracy concerning consolidated accounts specifying in article 8.1 that groups have to applied consolidation process beginning with 2005.

The inflation procedures still remained in the dark because "the annual financial statement will comprise all IAS except IAS 29. The companies who decided to apply IAS 29 will not reflect the adjustments made in accounting" [paragraph A1].

The IFRS application involved delicate issues concerning the accounting policies and methods companies have to become familiarly with. The first year application of IFRS

requested some specific demands, which shall be adopted by the companies. First of all, the financial statements have present comparative figures for achieving the issuing scope: to present as good as they can the results of the company's financial position. Also, the transition from the ex-accounting system to IFRS must be explained. As a consequence, companies will restate the financial statement for 2005 and 2004.

On the other hand, OMPF 306/2002, wanting to provide a simplified version of the international standards, doesn't have to do much with the European legislation and proves to be far too complicated, difficult to understand and adapt to the real situations in Romanian environment.

Another issue, brought out to light by such a comparison is that the Romanian legislation for SMEs and micro-enterprises maintains in the so-called simplified system elements that don't belong there, such those concerning the financial, instruments, fair value, accounts consolidation, groups of companies, and well as cash flow statement. Because these micro-enterprises do not have any intention whatsoever to be listed on the capital markets, to issue shares or form of a group, the above mentioned elements are completely useless and sometimes confusing.

Therefore, must be underlined the fact that the Romanian standard setter responded first of all to the Romania's political, economic and social needs to fit in the European accounting landscape so it can join the European Union, and only then to the need for accounting transparency required by the globalisation of the capital markets. In this situation, the prime user of the financial information shouldn't be the State anymore, but the investors as essential part of the development of the stock exchange.

However, by the endorsement of the latest regulations OMFP 1752/2005 Accounting Regulations in accordance with the European Directives, which should become effective 1st of January 2006, OMPF 94/2001 and OMPF 306/2002 will be abrogated. This bill refers to:

- The Fourth Directive of EEC with all the subsequent amendments;
- The Seventh Directive of EEC with all the subsequent amendments;
- The Directive 2004/25/EC of the European Parliament and of the Council of 21st of April 2004 about the bidding offers.

But even if OMPF 1827/2003 preceded this law, regarding the approval of the categories of companies that beginning with 2005 will apply IFRS in full; its issuance still came as a surprise for the majority of the practitioners. Romania's year 2006 will belong exclusively to the European accounting Directives and IFRS will be applied in full starting with 1st of January 2007 in parallel with the regulations in accordance with the European Directives.

The intention to adopt the latest legislative act Accounting Regulations in accordance with the European Directives represents a turning point for the evolution of the Romanian accounting harmonization process as well as the application of IFRS starting 1st of January 2007 for the companies complying with OMPF 1827/2003. Also, can be observed that the Romanian setting body didn't make a delimitation of companies according to their size and listed/unlisted quality. Starting 2007, the implementation of IFRS will face obstacles that risk to transform in serious difficulties for the convergence process, making necessary, on one hand, the active involvement of the accounting profession in the standards practical application, training of the specialists and elaboration of professional guides and, on the other hand, the development of the capital markets.

3.3 Current Romania auditing system

Like accounting regulations, audit standards and practice in Romania have been undergoing a process of change that is still developing. The Romanian Chamber of Auditors was established by Ordinance 75/1999 (as subsequently approved by Law 133/2002) to establish auditing standards in Romania and to monitor the audit profession in relation to membership and qualification standards including establishment of examinations and membership criteria, ongoing training programmes, ethical standards, and quality review procedures. The Chamber of Auditors has adopted for application in Romania the International Standards on Auditing as issued by the International Federation of Accountants.

In time there were defined a number of possible audit requirements:

- a) For completing financial statements under MoF Order 94/2001 the company must have financial statements audited by a "financial auditor", member of the Romanian Chamber of Auditors. The "financial auditor" issues a report to shareholders on the MoF Order 94/2001 prepared financial statements at the annual general meeting of shareholders.
- b) For SA (Joint-stock) companies that are not completing financial reporting under MoF Order 94/2001 a financial auditor or a "Censors Committee" as defined under Law 31/1990 (the Company Law) are required. A report is issued by the Censors Committee (jointly or individually) on the annual statutory financial statements to the annual general meeting of shareholders.
- c) If a SRL (limited liability company) has more than 15 shareholders, then a Censors Committee is required.
- d) For listed companies, the annual financial statements must be audited by a financial auditor. The report that is completed by the financial auditor is issued to the shareholders and to the Romanian Securities Commission. Companies completing MoF Order 94/2001 financial statements can have the same auditor for both financial audit reporting and CNVM reporting (National Securities and Exchange Commission) as long as the relevant "financial auditor" has an additional CNVM approved qualification (CNVM Instruction 4/2000).

4 Conclusions

The challenges faced in Romania at the commencement of the process of adoption of IAS cannot be overestimated. A refocusing of financial reporting to meet the demands of other users of financial information, such as shareholders, potential investors, customers and suppliers was required. The consequent application of an accounting framework based on use of judgment, with provision of additional disclosures and an acceptance that significant differences between accounting profits and fiscal profits control exist demanded a very significant change in accounting practice.

A change in mind set was also needed to overcome the past reluctance of preparers of financial information to disclose more than was absolutely necessary, in particular in relation to contingent liabilities (including liabilities to State organizations), related parties identification, and disclosure of certain segmental information.

The approach adopted by M.P.F. to address those issues can best be described as gradualist.

Not applying the inflation accounting and consolidated accounts, as generated by the permissive legal framework, and considering the implementation of all IAS, determined a faulty reporting of the economic reality, by maintaining the value of own capital in historical costs, the lack of validation of the values of patrimonial assets set up in accordance with specific standards, correlated to reporting a result of the financial year entirely irrelevant

from the point of view of its worth. We have to become aware that a compliance of financial situations to IASB can be realized only if the International Accounting Standards are applied all in all.

Now, the real challenge facing Romanian accounting is not accelerating introduction of reforms still needed, but policing those reforms already in place. Responsibility for policing does not lie with M.P.F. but rests with bodies such as the Romanian National Securities Commission, the Bucharest Stock Exchange and the auditing profession.

One major problem for Romanians accountants is the usefulness of a one clear rule, issued by Ministry of Public Finances, since IAS do not require entities to observe only one rule, but allows them to choose between alternatives. The Romanians practitioners have a huge fear to make chooses, because they haven't experience, they couldn't preview the consequences of one or other options, they really didn't know which is the best options for reflect the true and fair view of company financial position and performance.

At this point, we have to specify that Romanian accountants, probably more than other accountants confronted with the IAS application over the world, had to realized theirs mentality was not fitting well at all with the rules, principles and let's say the philosophy of IAS, and they are very skeptics. On the other hand, the students from our University, Babes Bolyai Cluj Napoca, are much more opened to understand and accept IAS or IFRS than accountants (IAS is part of Babes Bolyai University curriculum since 2000.) More over, they quickly assimilate the information received and take it as something is normal to be done. This tells us the battle isn't lost at all. At this moment we have to focus our attention on the middle age accountants, because they will be on the market for at least 10 or 15 years from now. If they continue to adopt the same attitude as far, neglecting the real benefits of something that give us the real picture of a company financial situation, the Romanian accountants have to reconsider their position on that matter.

Problems of using IAS observed during this research mostly refer to the excessively general nature of directions, there imprecision, lack of distinctness and of possible solutions for some fields, etc. Almost 70 % of respondents in the observed sample think that IAS is not precise enough for the practical use and are inadequately understandable (almost 30 %). To illustrate the problem that appears in the real accounting practice, here are some comments of respondents:

“IAS/IFRS should be more clearly explained and more accessible to a wide number of users... they contain too many compromises and alternatives... lots of questions have not been solved, some things have only been fundamentally solved and that gives the possibility of different individual interpretations... poor and inconsistent translations, etc.”

The majority of examinees (70 %) think that IAS/IFRS are god framework (base) for the choice and use of accounting politics, in other words, for making financial statements, but they should be in a certain way approached according to the needs of Romanian companies. In such context, the best way of approaching is by the opinion of examinees (almost 75 %), establishment of own accounting standards, which will be based on direction of International Standards. But in the same, time they will esteem our specific qualities, which mean they will be more specific, understandable and simpler for the use in our conditions.

In this point The Body of Accounting Experts and Licensed Accountants from Romania was active, positive by organising training courses and issuing guidelines.

Also, for listed companies, Bucharest Stock Exchange request the appliance of Corporate Governance Principles and National Securities Commission impose a minimum set of financial information to be delivered by listed companies.

The use of non transparent financial reporting, if we will adopt IFRS in the same manner like we did with IAS, enables some companies' management to conceal their true financial position, use of cash and periodic results from outside interested parties: not just existing outside shareholders, but also employees, creditors, prospective investors and local and federal government agencies and others. The application of IFRS will not of itself necessarily prevent major frauds and improper transactions for personal gain by management against its enterprise, but it will assist in their timely detection and will also act as an important deterrent.

Financial statements present financial and performance position in running a business. They are one of the determinant keys in the process of making investment decisions of both domestic and foreign investors. Because of these particular reasons financial statements have to be made in a way that would be understood by the capital markets, by all potential investors no matter which country they come from.

The capital markets includes a very broad group that includes all potential investors and lenders; organized stock markets, venture capital, banks, industrial partners and international institutions such as the ERBD. So, what the markets are looking for is high quality financial information, which possesses a number of desirable characteristics. That information should be comparable, so that the financial performance of different companies in similar business sectors is reported using the same accounting principles. Also, a company's own performance across several years must be comparable so that trends can be seen and understood. Financial information should be comprehensive, so that the reader can find all-important aspects of the companies' financial performance and position discussed. It should be fair, such that the information gives a fair representation of the economic reality of transactions and events. And finally it should be reliable. Investors can trust only reliable financial information. High quality reliable audited financial information is the lifeblood of the capital markets.

IAS and IFRS are our today's reality. Legislation should create a favorable environment to support IFRS adoption by companies, and provisions that would otherwise prevent or act, as an impediment to IFRS adoptions by enterprises should be changed. Therefore, as recognized above, companies which will prepare IFRS financial statements should be obliged to take into account all economic aspects present in the economy they run business. Do not forget that IFRS are prepared to meet and serve the needs of investors and other users of financial statement.

Also, wide-ranging Guidance, model examples and explanations of how companies can apply IFRS in practice are needed and should be widely disseminated.

IFRS signifies a new era of financial reporting that will touch thousands of companies around the globe. The fact that a vast majority of countries have an active agenda or IFRS convergence is very encouraging, but there is still much work to be done. All market participants such as governments, regulators, companies, and academic world should work together in the field of responsibility to further convergence.

Undeniable, IFRS provide higher quality information, more transparency and consistency, so the company's financial statement will be comparable both in time and space. More over, the Board encourages companies to apply IFRS rigorously. What does it imply? Do we not take into consideration specific differences that can arise in a particular geographic area? We don't think so, because the Board position is "standards will be applied without differences and interpretation". On the other hand, IFRS accept the existence of specific differences, depends the country. So, what does the acceptance and adopting IFRS totally, like the Board issued them, mean? This means that financial statement will look alike everywhere, in any country. The companies will report their financial statements according IFRS by presenting

the same thing, without any selection or options to reconsider. We can conclude particular differences can create confusions, as we demonstrated before, taking Romania case as example.

References:

- [1] BDO, Deloitte Touche Tohmatsu, Ernst&Young, Grant Thornton, KPMG, PricewaterhouseCoopers, GAAP CONVERGENCE 2002- A Survey of National Efforts to Promote and Achieve Convergence with IFRS
- [2] Can Simga-Mugan, Nazli Hosal-Akman -Convergence to international financial reporting standards: the case of Turkey, Int. J. Accounting, Auditing and Performance Evaluation, Vol. 2, Nos. 1/2, 2005.
- [3] CHANDLER, R. A. (1992) 'The international harmonisation of accounting: in search of influence', The International Journal of Accounting, Vol. 27.
- [4] DAY, J., TAYLOR, P. Accession to the European Union and the Process of Accounting and Audit Reform, Journal Accounting in Europe, vol2, 2005.
- [5] DELVAILLE, P., EBBERS, G. and SACCON, C. (2004) European Convergence to IFRS: Evidence from Three Continental European Countries in the Preparation for 2005, European Accounting Association, Annual Meeting, Prague, April
- [6] GOELTZ, R. K. (1996) 'International accounting harmonisation: the impossible (and unnecessary) dream?', in Blake, J. and Hossain, M. (Eds.): Readings in International Accounting, Thompson Business Press, London, UK
- [7] IASB – International Financial Standard Board, IFRS 1
- [8] IASC - International Accounting Standards, Economica, Bucuresti, 2002.
- [9] PriceWaterhouseCoopers (2002) PricewaterhouseCoopers 2005-Ready or Not, www.pwcglobal.com/ias.
- [10] PriceWaterhouseCoopers - Understanding IAS
- [11] STREET, D. L. (2003a) GAAP Convergence 2002, published by BDO, Deloitte Touche Tohmatsu, Ernst and Young, Grant Thorton, KPMG, PriceWaterhouse Coopers, February.
- [12] TIRON, T. A., MUTIU, I. A. Problems faced and solution developed during the implementation of IAS/IFRS – Romanian experience, 1st International Accounting Conference: On the way to Convergence, Accounting Academicians' Collaboration Foundation, 2004, Istanbul, Turkey
- [13] TIRON, T. A., MATIS, D., MUTIU, I. A. Looking to the future: IFRS – A common language for worldwide auditors and accountants? Proceedings of International Conference, Szent Istvan University, Hungary, 2004 sites.
- [14] www.asb.org.uk
- [15] www.contab-audit.ro
- [16] www.ey.com
- [17] www.iasc.org.uk
- [18] www.iasplus.com
- [19] www.icar.ru
- [20] www.ifac.org
- [21] www.pwcglobal.com

Contact:

Adriana Tiron Tudor, Associate professor, Ph.D.
Economic Faculty, Babes Bolyai University, Cluj Napoca, Romania
Cluj Napoca, Muscel Street no. 21 apt. 11
Phone: 0040744779474
email: ttadriana@yahoo.com