

previously permitted.

The project is intended to promote an international accounting language and thereby enhance understanding by all parties. This should improve investor confidence and thereby facilitate the flow of international investment.

Benefits of uniform international standard

- The elimination or reduction of differences between accounting standards would eliminate the need for the preparation of financial statements in accordance with several (different) accounting standards. This would result in the reduction (or elimination) of additional costs and administrative procedures.
- Reducing the diversity in accounting standards would result in the elimination of the reconciliation between GAAP of the local country and GAAP of the foreign parent company. (The greater the differences in GAAP between the countries, the higher the costs). The elimination of this reconciliation would also result in the reduction of costs.
- Eliminating diversity in standards would lead to increased comparability of financial reporting throughout the world. Genuine international investors are now fairly common, and the ability to directly compare financial reports from different countries can only enhance the flow of international investment.
- It is presently not possible for a company in a member state to transfer its registered office to another member state. Such negotiations can only be successful if there is enough harmonisation. The present absence of harmonisation has resulted in an uneven playing field for mergers and acquisitions.
- Reducing the diversity of accounting standards will result in all parties involved obtaining a better understanding of the reasons behind the differences. This should result in an improvement in the overall level of financial reporting.
- Failure to reduce the diversity in accounting standards may impact negatively on investor confidence. Hugh Collum, Chief Financial Officer of Smith Kline Beecham once said that

if you lose investor confidence, you lose a vital raw material of your business.

- The synchronisation of the present diverse accounting standards should go a long way to improving the uniformity of auditing, which should in turn, improve international investor confidence.

*To be continued in the next issue of
PODIUM*

TO HEDGE ACCOUNT OR NOT TO HEDGE ACCOUNT?

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PART 2

Problems encountered with hedge accounting

In terms of AC 208 a financial instrument can be used either for hedging (non-trading) or for speculative (trading) purposes. The substance of a hedging instrument is, however, not evident from or determined by its form but is based partly on management's intent. Therefore, a requirement for the use of hedge accounting is that management should designate the relationship as a hedge. Management's intent, without substantial supporting evidence, is not an ideal means of identifying a hedge as this can result in various forms of creative accounting. A distinction should perhaps be made between management's intent in entering into a hedge (economic intent) and management's intent in drafting the financial statements (reporting intent). Reporting intent may mask or even drive economic intent resulting, for example, in the creation of uneconomic or counter productive hedges. The susceptibility of an accounting treatment to creative accounting does not however provide sufficient grounds to prohibit its use. Users should nonetheless be aware of the increased risk that information relating to hedges may not be free from bias.

Comparability may also be impaired if the application of traditional accounting or hedge accounting is based on the intent of management. For example, two companies may each have a similar hedge and may also have the economic intention to reduce their risk exposure. The first company may designate the transaction as a hedge and will use hedge accounting. The second company, by contrast, may not designate

it as a hedge and will therefore use the traditional accounting approach. This is clearly contrary to the Mission Statement of the FASB which indicates that they are committed to:

"Developing neutral standards that result in accounting for similar transactions and circumstances similarly and for different transactions and circumstances differently".

It is apparent that the circumstances and economic intent should determine the method of accounting. Optional methods for both similar circumstances or similar economic intent destroy comparability. Greater comparability can probably be achieved by prohibiting or requiring hedge accounting under specified circumstances. A conflict sometimes exists however between presenting comparable information or relevant and representational faithful information. Improving comparability may destroy or weaken relevance or reliability if to secure comparability between two measures, one of them may have to be obtained by a method yielding less relevant or less reliable information. Financial reporting should strive to remain relevant and representational faithfully even if this is achieved at the expense of comparability.

Hedge accounting results in the offsetting of gains and losses whether these are realised or not. The IASC concluded that offset in the balance sheet should only take place when an enterprise has a legally enforceable right to set off the recognised amounts. It can be argued that the principles of offsetting should also extend to the income statement and that it is therefore improper to offset counterbalancing gains and losses. The counter argument is that the concept of substance over form should also apply to offsetting. Set off should be allowed where the economic substance of the transaction warrant offsetting to produce useful information. Consequently the argument concludes that the offsetting of gains and losses in hedge accounting should be permitted in order to reflect the economic reality of risk mitigation. The issues to consider is whether such offsetting will result in the loss of useful information and whether the disclosure of supplementary explanatory information may be sufficient to enable the user to make a proper evaluation.

Conclusion

Hedge accounting merely provides a means of "patching up" deficiencies in our current

accounting system. Tim Hagan used the analogy of accounting and a patchwork quilt at the 75th Anniversary Research Lecture of the New Zealand Society of Accountants:

"So what we must do in the interim is to continue on building the patchwork quilt without any real idea of how long or wide it should be or in fact how warm we wish it to keep us".

An ad hoc or patchwork approach can only serve as an interim measure. The deficiencies in the conceptual framework, especially the lack of consensus on measurement, will finally have to be resolved. Perhaps the current projects on financial instruments of standard setters in the United States of America, Canada and the IASC will contribute towards greater consensus by addressing some of the unresolved issues.

DEBATSVOERING

INTERNE OUDITKUNDE : ONS MISKENDE DISSIPLINE?

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DEEL 1

By 'n nadere ontleding van die onderrig-programme in die ekonomiese fakulteite van universiteite en teknikons in Suid-Afrika, in die algemeen, is dit opvallend dat die vak interne ouditkunde nie 'n volwaardige plek, soos die mede-dissiplines, finansiële rekeningkunde, ouditkunde, belasting en koste- en bestuurs-rekeningkunde het nie. Verskeie redes kan moontlik vir hierdie situasie aangevoer word. Die eerste en waarskynlik gewigtigste rede kan gesoek word in die feit dat interne ouditkunde eintlik as 'n ondergeskikte dissipline van ouditkunde beskou word en dat behoorlike kennis van laasgenoemde sommer ook voldoende kennis van interne ouditkunde veronderstel. 'n Tweede oorsaak wat tot interne ouditkunde se minderwaardige plek as vakdissipline bydra is die verkeerde persepsie dat interne ouditkunde slegs op kontrolering van die finansiële funksie van 'n besigheid toegespits is. Die derde rede waarom interne ouditkunde 'n miskende dissipline by tersiëre inrigtings in Suid-Afrika is, kan moontlik aan onkunde toegeskryf word. Onkunde oor die feit dat topbestuur in die privaat- en openbare sektor onder soveel toenemende druk verkeer dat die interne ouditfunksie, in die hele opset, nie net as