

## РОЗВИТОК ПАРАДИГМ ТА ТЕОРІЇ БУХГАЛТЕРСЬКОГО ОБЛІКУ: ЕВОЛЮЦІЙНИЙ ПІДХІД ТА ПОДАЛЬШИЙ ГЕНЕЗИС ОБЛІКОВОЇ ДУМКИ

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### TRANSPOSITION OF DIRECTIVE 2013/34/EU IN THE REPUBLIC OF BULGARIA - CHALLENGES, PROBLEMS AND POSSIBLE SOLUTIONS

#### *Abstract*

*The Republic of Bulgaria is currently in a period of transposition of Accounting Directive 2013/34/EEC. The emphasis in this article is put on the basic problematic areas which occur in the process of transposition of the Directive. Being based on the established traditions and practices, the author of this article tries to mark the possible solutions to these problems taking into consideration the requirements imposed by the Directive itself. Three principal problems are defined in the article: should there be a new Accounting Law and what should it include; should the Accounting Law include accounting principles; what groups and categories of enterprises should be differentiated.*

*Keywords: harmonization; accounting directives; accounting law.*

During the latest decades, two concurrently running processes – harmonization and convergence – have been exerting their influence on the conceptual fundamentals of the regulatory accounting framework in Bulgaria.

*Harmonization* is above all associated with the European Union (EU) Member States, as far as this notion is used in the context that the national accounting legislation of these countries should comply with the course laid down in EU Directives. This role of harmonization is a logical result of the fact that the accounting regulations in EU come in the form of Directives, the principal aim of which is the harmonization of legislation and accounting practices of the Member States within the Community. Two Accounting Directives<sup>1</sup> and one Regulation<sup>2</sup> of the European Parliament have the most substantial influence on the regulatory framework in the Republic of Bulgaria. In 1995, the European Union supported the International Accounting Standards Board (the Committee) for the establishment of global accounting standards and for the adoption of a strategy on the affiliation to the

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<sup>1</sup> The Fourth Council Directive of 25 July 1978, based on Article 54, paragraph 3, item (g) of the Treaty on the annual accounts of certain types of companies (78/660/EEC); and the Seventh Council Directive of 13 June 1983 based on Article 54, paragraph 3, item (g) of the Treaty on consolidated accounts (83/349/EEC).

<sup>2</sup> Regulation (EC) №1606/2002 on the application of IAS. Pursuant to Regulation (EC) № 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards by the companies whose securities are admitted to trading on a regulated market of whichever Member State. These companies should prepare their consolidated accounts in conformity with IFRS, and are subsequently exempt from the most of the requirements established in Directives 78/660/EEC and 83/349/EEC

provisions of the International Accounting Standards. Several documents (Regulations), including Regulation 1606/2002 on the application of international accounting standards in the preparation of consolidated financial statements, were published in consequence of this decision. Regulation 1606/2002 made the International Financial Reporting Standards (IFRS) mandatory only with respect to consolidated financial statements of entities whose securities have been registered for trading in the European securities markets. By adoption of this Regulation, EU officially joined the process of *convergence*. *Convergence* is considered to be a process of approximation of the American Generally Accepted Accounting Principles ( USA GAAP) and the International Accounting Standards (IAS /IFRS). We could say that its emergence is a logical result of professional accountants' striving for outlining and implementation of a permanent conceptual framework. Convergence aims at financial statements unification and establishment of uniform global accounting standards under the guidance of a Global Organization. The latter, in the words of Robert Herz<sup>3</sup>, is going to be a synthesis of the International Accounting Standards Board and the US Financial Accounting Standards Board. Convergence is identified as a very useful process which promotes the free flow of global investments and creates significant benefits for all the participants in the capital market. It improves investors' abilities to compare investments on a global scale, thus diminishing the risk of mistakes in their judgments. On the other part, convergence is regarded as a process which has a potential to create a new standard and greater transparency which are valuable for all market participants. Last but not least, convergence creates unprecedented opportunity for the organizations that determine the standards and the remaining powerful participants in capital market to enhance the accounting models applied by them. The guiding role of this process is currently supported by a variety of authoritative institutions. For example, the Members of the Financial Crisis Advisory Group specify that the issues concerning the accounting standards convergence and the independence and responsibility of issuers of accounting standards are brought to the front. At the same time, there are viewpoints which undervalue that role. For instance, the Members of the European Federation of Accountants believe that the focal point should move from convergence to improvement (simplification) of standards. The reasoning provided by them states that the key differences have been smoothed out, the approximation on significant issues is under way, and that only insignificant matters remain to be resolved. In our point of view, it is difficult to assume that the role of convergence has been exhausted. In favour of this thesis one could provide the reasoning that at this stage it can not be definitively asserted that convergence has reached its aim - i.e. the establishment of a common accounting model, built on accounting standards based on principles. Due to that reason, all users, which rely on the information from the financial statements, should understand the questions related to approximation, should shape a statement and take time to participate in the global debate. The most important issue in this moment is to arrive at high-grade similar standards which are to be equivalent to a considerable degree, however not the same in every detail. The primary issue at a later stage will probably be the matter concerning the unified high-grade global standards and the common

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<sup>3</sup> Chairman of the US Financial Accounting Standards Board ( FASB)

organization which is expected to set those global standards. The main problem, which however still remains to be solved, is the choice between standards based on rules and standards based on principles.

In 2013, the Fourth and Seventh Directives were replaced by a new Accounting Directive – Directive 2013/34/EC. The Directive is the outcome of EU aspirations to relieve the business environment of small and medium-sized enterprises by simplifying the requirements with regard to reporting and mandatory disclosures for that category of enterprises. The entities of the practical sector (public and private limited liability companies, partnerships, general partnerships, etc.) come within the scope of the Directive. The scope of the Directive excludes non-profit legal entities. The provisions of the Directive should for the first time be applied with regard to financial statements for reporting years beginning on or after January 1, 2016. Being an EC Member State, the Republic of Bulgaria has to transpose the Directive into the national accounting legislation by July 2015. Several groups of principal questions arise in connection with its transposition.

*First: Should there be a new Accounting Law and what should it look like?*

In Bulgaria, the material and procedural issues of accounting were for the first time institutionalized in law in 1991, when the Grand National Assembly adopted the Law on Accounting (AL) on 03.01.1991. The stipulations of the Fourth EU Directive were adopted to set the grounds of the first Accounting Law. The National Chart of Accounts<sup>4</sup>, whose drafting involved the organization of the chart of accounts of France, was adopted during that period as well. The first National Accounting Standards (NAS), with the general provisions of the International Accounting Standards grounded in their fundamentals, were adopted in 1993. Since 1991, a multitude of amendments and changes to the regulatory accounting framework have been made, and particularly frequent have been the amendments to AL, for the purpose of achieving harmonization with the European Directives and IAS. Two financial reporting bases have been introduced in the Republic of Bulgaria for the preparation of financial statements of enterprises – IAS (IFRS) and NFRSSME. Steps were taken to divide the enterprises in the Republic of Bulgarian into two groups - the group of „small and medium-sized undertakings”, which apply the national accounting standards<sup>5</sup> (with the possibility to apply IAS(IFRS) at their own discretion) and the group of “large undertakings”, which are obliged to apply IFRS.

The prevailing opinion<sup>6</sup> at present is that the transposition of Directive 2013/34/EEC should be tied down to the adoption of a new Accounting Law. However there are standpoints<sup>7</sup> according to which separation of accounting from business should not be allowed and all procedural issues concerning the system of accounting

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<sup>4</sup> In 1998, the application of the Unified National Chart of Accounts was repealed, and that was connected with the tighter linking of the accounting system in Bulgaria with IAS, standards based on principles.

<sup>5</sup> By virtue of ORDINANCE № 46 of the Council of Ministers of 21.03.2005, the National Financial Reporting Standards for Small and Medium-sized Entities (NFRSSME) were adopted. These new accounting standards were promulgated in State Gazette, issue 30 of 7.04.2005, effective as of 1.01.2005 and are intended for small and medium-sized enterprises.

<sup>6</sup> The Accounting and Finance Department at the University of National and World Economy organized a roundtable discussion on the theme “Aspects in the development of the regulatory accounting framework in Bulgaria” held on 17.03.2014, where some leading scientists in the field of accounting theory and practice developed that thesis.

<sup>7</sup> See. Svrakov, A. „ Nyakoi idei pri sazhdavane to na kontsepsiya za razvitiye na schetovodno zakonodatelstvo v Bulgariya”, IDES,2014. (Some ideas when establishing a concept for the development of accounting legislation in Bulgaria, Institute of Certified Public Accountants)

should find their place in the Law on Commerce (CL)<sup>8</sup>. The main argument in defense of this thesis is that accounting is not just a technique, it is trader's quality, and being such, it should find its place among the legal norms of Chapter VII Commercial Records of the Law on Commerce. The foremost advantage of this position, in our point of view, is that the fundamental contradiction between some stipulations of Directives and IAS (IFRS), which exists in the effective regulatory accounting framework, will thus be overcome, and it will be possible to approve the generally accepted statutory accounting regulations. From another perspective, thus we will turn to the old German practice, well-studied in our country years ago. The adoption of such an approach would also lead to overcoming of problems<sup>9</sup> associated with the application of the going concern principle as a principle in trading and law (not only an accounting one); to better and clearer understanding of the stipulations on revaluation and impairment of assets, as well as the stipulations concerning consolidated statements. Notwithstanding the advantages of such an approach, we are quite skeptical with regard to the realization of this position. This skepticism originates above all in the comparatively short time limits within which the Directive should be transposed in Bulgaria and the practices that have been established over the latest twenty years.

As to the contents of the Accounting Law, there should be an agreement achieved on the following questions: Should the new law reproduce the arrangements and stipulations of the preceding one and should it involve provisions concerning budgetary enterprises? The opinions on these issues are different.

As long as Directive 2013/34/EU contains provisions of the consolidated Fourth and Seventh Directives, provisions which found their reflection in the applicable Accounting Law over the years, it is more appropriate to preserve the logics and the structure of the so far effective Accounting Law to a great extent. There should be a regulation of the accounting process of budgetary enterprises and most properly it should be set in a distinct, separate chapter of the Accounting Law. In our point of view, such issues as: organization of the accrual-based accounting system; building and maintaining the accounting system of enterprises; accounting documentation, inventory count of assets and liabilities; storage of accounting information; applicable accounting basis and financial statements; measurement and presentation of accounting items; categories of enterprises; business reports and reports on payments to governments; issuers of financial statements; publicity of financial statements and independent audit of financial statements, should find their place in the new Accounting Law. The Accounting Law should definitely involve regulatory provisions on audit reports concerning payments made by mining or timber industry enterprises to the government. This type of reports will be required to be provided by public-interest entities and large entities operating in those spheres of business. Thus, it will be possible to achieve the transparency required by the Directive on the payments which the respective States receive as a consideration for the rights granted on the use of natural resources.

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<sup>8</sup> This formulation is new. From 1898 to 1944, the Bulgarian Law on Commerce involved the material and procedural issues of accounting.

<sup>9</sup> See. Svrakov, A. „Nyakoi idei pri sazdavaneto na kontsepsiya za razvitie na schetovodno zakonodatelstvo v Bulgariya“, IDES, 2014. (Some ideas when establishing a concept for the development of accounting legislation in Bulgaria, Institute of Certified Public Accountants).

*Second: Should the Accounting Law incorporate accounting principles and which of them should be included?*

The definition of accounting principles in the Accounting Law allows their easier understanding and application on behalf of the issuers of accounting statements. The question of accounting principles is quite delicate since there is no single and distinct position on what an accounting principle<sup>10</sup> is. Traditionally, the accounting principles are brought to generally accepted assumptions, which are applied in the preparation of financial statements. For the purpose of overcoming this problem, usually the accounting principles are supplemented by suggestions and requirements. The main deficiency of such an approach is that it is not specified what exactly a principle, suggestion or requirement is. The Accounting Law should at least reflect the going concern concept, prudence concept, principle of accrual-based accounting, and substance over form principle, adopted in the Directive.

*Third: What categories of enterprises should be identified and which accounting basis should be applied by any of them?*

Directive 2013/34/EEC introduces harmonized criteria on "micro", "small", "medium-sized" and "large" undertakings, and the definition of the separate categories is based on the balance sheet total, net turnover and the average number of employees. Unfortunately, when being defined, no account has been taken of the magnitude of the respective economies in the Community. On the other hand, the Directive provides an option for the large States to raise the criteria for small enterprises, while an option for the small States to reduce these criteria has not been given. Four categories of undertakings could be differentiated in the Accounting Law, according to the requirements of the Directive. Departing from the specifics and the magnitude of our economy, the following groups could be identified. The first group of undertakings is the group of "small" entities, which is supposed to include micro-undertakings and part of the small enterprises (within the meaning of art. 3, par.1 and par.2 of the Directive). Basically this group will include entities which, within the meaning of the currently effective Accounting Law, apply simplified accounting<sup>11</sup>. They will benefit from such exemptions as: condensed balance sheet; no requirements on preparation of annual activity report and compulsory independent audit. The second group will include undertakings with indicators above those of "small" entities up to the criteria, as specified in art. 3, par. 2 of the Directive. These undertakings will make use of the mandatory exemptions in the Directive. The third group is the group of medium-sized and large undertakings, which will cover all enterprises with indicators above those for small enterprises under the Directive. The fourth group is the group of public-

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<sup>10</sup> According to D. Zhelyazkov, the new Accounting Law should preserve the accounting principles grounded in the currently effective law, namely: going concern concept, principle of accrual-based accounting; prudence concept; matching of income and expenses concept; substance over form principle; preservation of accounting policies from prior accounting period; independence between accounting periods and correspondence between opening and closing balances. (See. Project of AL, ICPA); According to the workgroup of ICPA working on the development of a new AL, the following should be included: going concern concept, principle of accrual-based accounting; prudence concept; substance over form principle; preservation of accounting policies from prior accounting period; independence between accounting periods and correspondence between opening and closing balances; the elements of assets and liabilities items should be separately measured; no assets and liabilities, income and expenses should be offset; concept of materiality in presentation and disclosure of information.

<sup>11</sup> The criteria for this group are: 1.5 mln BGN of net book value of assets; 2.5 mln. BGN net turnover and personnel of 50 employees. The workgroup of ICPA working on the project for a new Accounting Law suggests that the criteria for this category should be increased by the official inflation rate for Bulgaria for the period 2007-2013.

interest entities<sup>12</sup>. The differentiation of this group is imposed by the fact that public-interest entities are set apart in a distinct category in the Directive, and an option is given for each Member State to expand the given definition. Enterprises whose equity instruments or debt securities are publicly traded; enterprises, which collect and manage substantial public resources, and entities which spend substantial funds of public budgets, should also be included in the group. Specifically, this group involves: financial institutions; investment undertakings; retirement insurance entities and pension funds; special investment entities; credit institutions and foreign bank subsidiaries; collective investment schemes; insurance and reinsurance companies; enterprises whose capital instruments are traded in the stock market, and non-profit legal entities, determined to pursue activities of public benefit.

The question concerning the basis of accounting, which will be applied by the respective groups of undertakings, should also be solved in the new Accounting Law. Our standpoint is that IAS (IFRS) should be applicable for public-interest entities and large undertakings, as well as by those undertakings which have by now adopted this basis. IAS (IFRS) should also be applied by small and medium-sized undertakings, which are parent companies of business groups, which comprise at least one public-interest entity. The new Accounting Law should provide a possibility for small and medium-sized enterprises to choose between IAS and NAS, as well as the possibility to change the initially recognized basis of accounting.

The transposition of Directive 2013/34/EEC in Bulgaria offers an opportunity to overcome a variety of contradictions in the currently effective regulatory framework, but at the same time this process generates a number of problems as well. In the process of finding solutions to those problems, we need to definitely take the business environment of our economy and the admissible deviations, stipulated in the Directive, into account.

#### References

1. Directive 2013/34/EEC of the European Parliament and of the Council of 26 June 2013.-OG, L 182/19 of 26.06.2013;
2. Accounting Law, SG, issue 98 of 2001, as amended issue 100 of 2013.



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<sup>12</sup> At the suggestion of V. Filipov from ICPA, small undertakings should have 7.8 mln BGN of net book value of assets; 15.6 mln. BGN of net turnover and average number of employees - 50 people; and medium-sized undertakings should have net book value of assets - 39 mln. BGN; net turnover - 78 mln. BGN and average number of employees - 250 people.