

Article

# Analysis of accounting standards: Preferences and effects on Hungarian holding companies

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**Abstract:** Entities that are members corporate groups prepare their individual financial statements independently of each other, according to their own national laws, but also according to one of the international accounting standards. It is the obligation of parent companies to prepare the consolidated financial statements, which represent the corporate group as one single company. For market operators, it is essential to compare the performance of different business entities, irrespective of different applicable national accounting rules. Users of financial statements need a uniform accounting system that makes the understanding of the content more transparent and clearer thus helping decision-making. In this study, the importance and legal background of consolidation are described, as well as the comparison of Hungarian and international rules on consolidation. Comparison by sectors includes data on sales revenues, data on employment and it also includes whether the choices made on accounting standards and the sectoral differences have an impact on the scores of the ESG-index.

**Keywords:** consolidation; consolidated financial statements; International Financial Reporting Standards;

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## INTRODUCTION

Multinational corporations operating within different economic and legal environments in the global economy have multiple connection systems. These enterprises through investments and cross-border transactions, establish relationships that bring them in a position of interest, ownership, and dependency (Jakus, 2015).

For market operators looking for investment opportunities and intending to invest it is essential to be able to compare their needs and opportunities. In case only financial statements prepared according to different national regulations are available, the performance of different business entities is hard to compare (Madarasiné Szirmai et al. 2019). There are significant differences between the accounting rules of different countries both in terms of content and form (Sztanó & Vörös, 2001). Users of financial statements need a uniform accounting system that makes the understanding of the content more transparent and clearer thus supporting decision-making.

The two major accounting systems that currently prevail and are internationally known and accepted are the US GAAP (United States Generally Accepted Accounting Principles) developed in the United States of America and IFRS (International Financial Reporting Standards). IFRS has converged towards US GAAP mainly in the field of consolidated reporting, but differences still exist between the two systems (Cîrstea & Baltariu, 2014). Entities that are members of corporate groups prepare their individual financial statements independently of each other, according to their applicable national laws and regulations, or one of the international accounting standards. At the same time, it is the obligation of the parent companies to prepare the consolidated financial statements that represent the corporate group as one single company – eliminating the influence of the transactions between entities in the group.

In this study, the importance and legal background of consolidation are described, as well as the comparison of Hungarian and international rules on consolidation for groups of entities. Furthermore, comparisons by sector are made among Hungarian parent companies that prepare their financial statements according to the Hungarian rules or IFRS. The analysis covers development of data on sales revenues and employment, and at the same time, on whether choosing the accounting standards (IFRS or Hungarian Accounting Act) and sectoral differences affect the development of the scores of the ESG index.

## LITERATURE REVIEW

### **The importance of consolidation**

It is essential for stakeholders (creditors, owners, investors, governments, etc.) to have access to financial statements that provide an accurate and true representation of the operations, assets, financial and income positions of corporate groups (Jakus, 2015). These individuals and organizations have different needs for information (Fenyves et al. 2015), and the available information serves as basis for further analysis, investigations, and decision-making processes; therefore, it is of crucial importance, that the provided information ensures a credible picture of the business (Dékán T-né, 2019; Zéman et al., 2016). It is the expectation of market operators that objective information on the financial situation and profitability of the company shall be easily available (Böcskei et al., 2015). Insufficient information means increased risk, especially for investors and creditors (Fenyves et al., 2018).

In order to present a reliable and true picture, it is necessary to interpret businesses that have ownership and equity relationships with each other as a single corporate group and apply the methods of consolidated financial reporting (Simon, 2009a; 2009b; 2010).

Most countries legislate that companies present reliable and true picture of their patrimony, protecting therefore the investors and creditors. Due to the relationships within the corporate groups, funds obtained from original external sources by them may be transferred to other entities within the group, that, based on their own individual financial information, may not be able to acquire such resources for financing their operations. Therefore, it is of particular importance for stakeholders to analyse not only the individual financial statements but also the consolidated financial statements of the corporate group, and only make decisions on establishing or continuing their relationships if the assessment of both statements is favourable together (Simon & Kresalek, 2017).

### **The legal background of consolidation**

In the legal system of the European Union, the application of regulations is mandatory for individual member states, as they directly become part of the national law. Council Regulation (EC) No 1606/2002 on the application of international accounting standards prescribes the compulsory use of International Financial Reporting Standards (IFRS) for the consolidated annual financial statements for companies listed on the stock

exchange within the European Union since 2005 (Bartha et al., 2013).

According to the Regulation (EC) No. 1606/2002, Member States may allow or require the aforementioned companies listed on the stock exchange to prepare their individual annual financial statements, as well as the consolidated annual financial statements of non-listed companies, in accordance with international accounting standards. Accordingly, in case of the consolidated financial statements of the companies listed on the stock exchange, Member States do not have an option, at the same time, they are free to decide in any other cases, i.e. when and among which companies they make it possible or compulsory to apply the international standards at their individual and/or consolidated levels, and which of them are left within their national accounting systems.

In Hungary, according to the above-mentioned Regulation (EC) No. 1606/2002, companies listed in the stock exchange are expected to prepare their consolidated financial statements according to the International Financial Reporting Standards (IFRS), and it is also an option for other companies as well. By the recent amendments to Act C of 2000 on Accounting (Act C of 2000 on Accounting, 2024), the legislators have tried to bring the domestic accounting system closer to IFRS, however, there are still significant differences between the two regulations, accordingly, not only individual financial statements but those at a consolidated level show significant differences if prepared by the two different methods.

### **Comparison of Hungarian and international consolidation standards**

Parent companies in Hungary are entitled to prepare their consolidated financial statements: according to the Hungarian Accounting Act or according to the international standards. Consolidated financial statements are made by large enterprises which typically have a high turnover and a high number of employees. At the same time, significant differences can be identified between sectors with respect to the average sales revenues per company and the number of employees.

With the amendments made to the Hungarian Accounting Act in recent years, the legislatures have been attempting to align the domestic reporting system with IFRS, though significant differences still exist between the two regulations, hence the financial statements prepared under the two different methods might show significant differences not only at an individual, but at a consolidated level as well. It will become increasingly important for companies to evaluate and measure their business activities

according to the principles of sustainability, especially because of the expectations of their financiers and customers. Nowadays, if a company presents a product or itself as sustainable, it can potentially realize significant benefits from it (Dobos & Major, 2024).

The Hungarian regulations on accounting are based on the realisation principle and focus on past valuation, whereas IFRS is characterised by time value principle and prioritises fair valuation (Simon, 2022). Hungarian regulations focus mainly on individual financial statements, while international standards were developed for consolidated financial statements (Lakatos et al., 2018).

IFRS decreases information asymmetry by increasing transparency and comparability of financial statements. (Ashbaugh & Pincus, 2001; Daske et al., 2008; DeFond et al., 2011; Karpuz et al., 2020). Standards might help enterprises in reducing non-transparency and this is especially important for companies not listed on the stock exchange, or for SMEs (Belletante & Levratto, 1995; Jappelli & Pagano, 2002; Jappelli et al., 2005; Haselmann & Wachtel, 2010; Bertrand et al., 2020).

Steps of consolidation are practically the same under the Hungarian and the IFRS system (Madarasiné et al., 2019), at the same time differences can be found between the two regulations concerning the implementation of consolidation, that are presented in the following based on Rózsa (2015), Lakatos et al., (2018), Madarasiné et al., (2019) and Simon (2022).

According to the Accounting Act (Act C of 2000 on Accounting, 2024) a parent company can be exempted from the obligation of preparing consolidated financial statements and consolidated business reports (exemptible parent company) if the parent company itself is an affiliated company of another company (superior parent company), if the superior parent company is established in any state of the European Economic Area, and it prepares and publishes consolidated its financial statements and consolidated business reports according to the Accounting Act or the IFRS, in which the financial statements of the exemptible parent company and its affiliated companies are also consolidated.

The parent company – except for credit institutions, insurance companies, and financial companies as parent companies – is not obliged to prepare consolidated financial statements on the business year, if any two indicator values of the following three do not exceed the following thresholds in two consecutive business years preceding the business year in question: in case of balance sheet total, HUF 6,000 million, in case of annual net sales revenues,

HUF 12,000 million, in case of average number of employees in the business year, 250 people.

Under IFRS, a parent company can only be exempted from preparing consolidated financial statements, if all of the following three requirements are met: the consent of the owner is required, the company is not listed on the stock exchange, the superior parent company prepares a consolidated financial statement.

In case of affiliated companies, the IFRS does not allow any exemption. At the same time, according to the Accounting Act, the affiliated company shall not be involved in the consolidation if: it was not able to develop the reporting system (in the first year of involvement), the share is listed among current assets, the parent company is prevented from exercising its rights by extraordinary circumstances, the company is under registration, the consolidated financial statement provides a true and fair picture without involving the affiliated company.

The two regulations are not uniform with respect to intragroup accounting policies either. Under IFRS, uniform accounting policies are mandatory, while under the Accounting Act, this shall only be pursued. It is possible that intragroup companies have different balance sheet reference dates. Under the Hungarian regulation, balance sheet date of the company involved in the consolidation shall be within three months, otherwise, interim financial statements are necessary. IFRS provides that a maximum of three months may go by between the two balance sheet dates, otherwise, interim financial statements are required under it as well.

The two systems are not uniform with respect to the definition of the date of first involvement as well. The Accounting Act provides that the capital consolidation differences shall be calculated either on the basis of equity values valid on the date of acquisition or on the first consolidation date, while IFRS only allows to calculate the capital consolidation differences based on the equity values valid on the date of acquisition.

Under IFRS, all steps of full consolidation are mandatory, and capital consolidation is possible by using the actualized value method, while the Hungarian regulations provide that the capital consolidation is mandatory, but consolidation of debt, revenues-expenses and interim results may be omitted based on the principle of materiality, and with respect to capital consolidation, either the method of the book value or the method of the actualized value can be chosen.

Under Hungarian accounting, active capital consolidation difference is generated, if the book value of the parent company's share in the affiliated company exceeds the amount due to the parent

company based on its ownership interest in the affiliated company. In the consolidated balance sheet, the active capital consolidation difference shall be accounted for separately within the invested financial assets. It occurs if the parent company buys the share at a higher value than the value of the own funds in proportion to the value of the share. There can be several reasons for this higher price, for example supposing hidden reserves, or surplus value that cannot be displayed as an asset (customers, market monopoly, established brand name on the market) within the affiliated company, or simply a bad deal, collectively known as goodwill. Planned depreciation shall be accounted for the active capital consolidation balance, but extraordinary depreciation is also allowed. Passive capital consolidation difference is generated, if the book value of the parent company's share in the affiliated company is less than the amount due to the parent company based on its ownership interest in the affiliated company. In the consolidated balance sheet, the passive capital consolidation difference shall be accounted for separately within the subordinated liabilities. The parent company purchases the share at a lower price if it supposes hidden burdens, potential losses arising later, or products of poor quality – collectively known as badwill – with respect to acquiring the shares. Of course, it can also simply be a good deal as well.

Under IFRS, goodwill (the difference between the purchase price and the net asset value) shall be accounted for as a separate item within the consolidated balance sheet, and an impairment loss test shall be made on a yearly basis with respect to it, but planned depreciation cannot be accounted for it. In case of negative goodwill (badwill), the first step is to review whether the assets and liabilities have been properly accounted for and valued, and if the result is the same following the review, then it shall be considered as a good deal (for example, when the seller accepts a purchase price under the real value), the amount of which shall be immediately accounted for the benefit of the results.

## METHODOLOGY

The author has collected primary data from two companies: the Service of Company Information and Electronic Company Registration of the Ministry of Justice, and Opten Ltd and also secondary data from the Hungarian Central Statistical Office. The data was collected for the reporting period 2021-2022.

The Service of Company Information and Electronic Company Registration of the Ministry of Justice

(Service of Company Information) has provided data on the number of parent companies disclosing their consolidated annual financial statements according to the Hungarian Accounting Act and with respect to IFRS in 2022. The disclosure includes only the TEAOR (NACE) numbers of the main activities and the tax numbers, thus data has been categorized and aggregated, and sectors have been identified based on this.

The issue of sustainability is a major research area nowadays, and the economic, environmental and social aspects of sustainability affect all economic operators (Böcskei & Vértesy, 2022). ESG is the abbreviation for Environment, Social, and Governance. The criteria provide information on the extent to which the company demonstrates environmentally and climate-friendly behaviour, how well it complies with aspects such as occupational health and safety, or the applied management and control processes (Dun & Bradstreet, 2024).

Opten Ltd. has also provided data: ESG indexes of companies disclosing a consolidated annual financial statement for the year 2022. At the same time, TEAOR numbers for the main activities were also available in the database. For some companies, the ESG index was not disclosed, these were omitted from the calculations. A covariance analysis was performed using the SPSS programme in order to decide whether the choice made on accounting standards (IFRS or Hungarian Accounting Act) and sectoral differences have an influence in the scores of the ESG index.

The Hungarian Central Statistical Office has also provided data: aggregated data on the consolidated balance sheets and income statements of the year 2021, grouped by national economic sectors, in which the parent companies are classified by their main activities. With respect to four sectors (Accommodation services, catering, Human health and social care, Art, entertainment and free time, Other services) no data was disclosed, thus they were omitted from the analysis.

The aim of the author was to examine all the parent companies operating in Hungary that prepare consolidated financial statements, so all such companies were included in the study, thus, the author examined the entire population.

## RESULTS

### Accounting preferences of the Hungarian holding companies

Based on the data disclosure of the Service of Company Information, 195 consolidated financial

statements were prepared as per the Hungarian Accounting Act in 2022. Companies preparing their consolidated financial statements according to the Hungarian regulations have performed their activities within 42 sectors based on their main activities. Most of the companies operate in financial intermediation, but the number of companies involved in business and management consultancy services, wholesale trade and real estate transactions is also significant.

In 2022, 54 consolidated financial statements were prepared based on IFRS, and this involves a lot less, 19 sectors. The sectoral distribution of the consolidated financial statements can be seen on Table No. 1. Most of the companies operate in financial intermediation, real estate transactions and wholesale. In the sectors of manufacture of food products, and crop production, animal breeding, wildlife management and related services 12 parent companies perform their activities in total, but within these sectors – similar to the data of 2018 (Dienes & Bács, 2020) – none of the companies have chosen IFRS accounting. This could be due to several reasons, including regulatory requirements, the scale of international operations or the complexity of financial transactions within these sectors.

### Data on sales revenues

Data of income statements of companies preparing consolidated financial statements in 2021 show that the highest net sales revenues can be found in the trading and motor vehicle repairment sectors, 30 companies generate HUF 87.5 billion income. The sector of transport and warehousing also has a significant sales revenue, 14 companies have accounted for HUF 26.8 billion income. The total value of the 17 companies engaged in real estate transactions exceeds HUF 16.4 billion. In general, the highest amount of sales revenues per company can be detected among trading and motor vehicle repairment, while activities related to water supply generate the lowest income among the national economic sectors. Most of the companies account for financial and insurance activities, but at a lower average sales revenue than in other sectors, for example in the construction industry or processing industry (see Table No. 2.).

### Data on employment

Employment data of companies preparing consolidated financial statements in 2021 show that the average number of employees is the highest within the transport and warehousing sector, which is 100,965 people. The financial and insurance sector follows behind with 48 companies with an

average number of employees of 31,272 people. Professional, scientific, and technical activities are also significant, as they employ an average of 19,680 people. Within other national economic sectors, for example within the trading, processing industry and real estate market, the average number of employees is lower, within trading and motor vehicle repairment, on average, 14,802 people are employed, while within the processing industry, they employ an average of 13,543 people. On average, the sectors with the lowest number of employees are electricity and water supply, and information and communications sectors (see Table No. 3.)

#### **ANCOVA results of the ESG index by accounting standards and sectors**

ESG Index, received from OPTEN Ltd., shows the ESG level of a company based on more than 75 parameters. This means an index number (Opten, 2024) from 1 to 10 based on the results of the environmental, social, and corporate awareness.

The results of the ANCOVA model, which examines ESG index by financial statement standards and sectors show a significant model fit ( $F(24, 220) = 3,518, p < .001, \eta^2 = .277$ ). The intersection point is highly significant ( $F(1, 220) = 2830,405, p < 0,001, \eta^2 = 0,928$ ), which indicates a strong overall effect. Applying IFRS (Hungarian Accounting Act coded 0, IFRS coded 1) is not significant ( $F(1, 220) = 0,345, p = 0,558, \eta^2 = 0,002$ ), that means it does not have a distinctive effect on the scores of the ESG index. Differences between sectors are significant ( $F(14, 220) = 2,987, p < 0,001, \eta^2 = 0,160$ ), which indicates that the sectoral differences have an effect on the scores of the ESG index. However, the sectoral interaction effect of IFRS is not significant ( $F(9, 220) = 1,545, p = 0,133, \eta^2 = 0,059$ ) indicating that the impact of IFRS does not vary by sector. The model explains 27.7% of the variance of the ESG scores, adjusted R-square is 0.198, indicating moderate explanatory power of the model.

The estimated mean value of ESG shows different results between companies applying the Hungarian Accounting Act and IFRS. In general, sectors such as water supply and construction industry show higher ESG according to Hungarian standards, while transport, warehousing and financial activities have higher values according IFRS. Accommodation services, administrative services, art, entertainment, and other services account for a high ESG value (in the later three sections, the financial statements are only made according to the Hungarian standards). The processing industry shows a significantly higher value according to the Hungarian standards that according to IFRS (see Figure No. 1.). On the whole this suggests that no consistent trend can be found in

ESG scores across sectors between the two accounting standards.

Among Hungarian parent companies, a transition trend to IFRS has already started. Before the analysis was carried out, the author assumed that companies would make a transition to international standards more slowly at a consolidated level, that is, the Hungarian accounting system is still preferred by the majority of the company groups. At the same time, there are industrial sectors where the presence of IFRS is strong. The analysis shows that most of the Hungarian holdings have not made a transition towards IFRS yet. This study is of a unique nature, even after lengthy research, the author did not find any studies explicitly aimed at choosing the accounting system of parent companies. In the future, it would be worthwhile to examine the proportion of foreign ownership, the share of state ownership and the export and import data within the companies as these factors might also have an impact on the choice of the accounting system.

#### **CONCLUSIONS**

The aim of the author was to present the importance of consolidation, its legal background, the comparison of Hungarian and international rules on consolidation, and to perform analyses with respect to Hungarian parent companies. The theoretical overview is followed by a comparison by sector among Hungarian parent companies, which prepare their consolidated financial statements according to the Hungarian regulations or the IFRS standards. The analysis also covered whether the choice made concerning the accounting standards and sectoral differences have affect the scores of the ESG index. The data collected shows that Hungarian holding companies clearly prefer the Hungarian Accounting Act to IFRS, which is reflected in their financial statements. This may be due to the high costs of the transition to IFRS, or if the Hungarian owners do not intend to open up to foreign partners (such as investors), they may still consider the application of international standards unnecessary. In some sectors, in particular agriculture and water supply, companies only use national standards, while IFRS is applied by a minority of the companies that tend to prevail within the financial sector. Those companies that are required by law to do so have already transitioned to IFRS.

The analyses show that the trading and repairment of motor vehicle sector had the highest sales revenues per company, and that the transport and warehousing sector had the highest average number of employees. The statistical analysis shows that the

IFRS does not have a significant effect on the scores of the ESG index across sectors. At the same time, if a company is planning to attract foreign capital, it is definitely worthwhile to apply international standards, which make the content of the financial statement more transparent and clearer, thereby helping decision-making.

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**Table No. 1**  
**Consolidated financial statements in 2022**

<b>Name of the sector</b>	<b>Consolidated financial statements - Accounting act (pcs)</b>	<b>Consolidated financial statements with IFRS (pcs)</b>
Financial intermediation (except for insurances and pension fund activities)	42	21
Business and management consultancy services	21	3
Wholesale trade (except for motor vehicles, motorcycles)	19	4
Real estate transactions	18	7
Construction of buildings	8	
Retail trade (except for motor vehicles, motorcycles)	8	
Warehousing, additional activities of transport	8	
Manufacture of food products	7	
Crop production, animal breeding, wildlife management and related services	5	
Special construction	5	
Supply of electricity, gas and steam, air conditioning	4	
Legal, accounting and tax consultancy services	4	
Waste management	3	
Trading and repairment of motor vehicles, motorcycles	3	
Land transport and transport via pipelines	3	3
Engineering and architectural activities: technical examination, analysis	3	
Forestry	2	
Manufacture of pharmaceuticals	2	
Manufacture of rubber and plastic products	2	
Construction of other structures	2	
Information technology services	2	
Other financial activities	2	2
Advertising, market research	2	
Other professional, scientific, and technical activities	2	
Other sectors	18	14
<b>Total</b>	<b>195</b>	<b>54</b>

*Source: own editing based on data provided by the Service of Company Information and Electronic Company Registration of the Ministry of Justice.*

**Table No. 2**  
**Number of companies submitting consolidated financial statements and data on average sales revenues, 2021**

<b>Name of the sector</b>	<b>Number of companies (pcs)</b>	<b>Average sales revenues (mHUF)</b>
Trading and motor vehicle repairment	30	2 918
Transport and warehousing	14	1 915
Real estate transactions	17	966
Professional, scientific, and technical activities	31	109
Financial and insurance activities	48	39
Construction industry	11	77
Processing industry	20	41
Administrative and service support activities	4	82
Information, communication	4	79
Agriculture, forestry and fishing	6	44
Supply of electricity, gas and steam, air conditioning	4	21
Water supply, waste water collection and treatment, waste management, pollution control	3	14

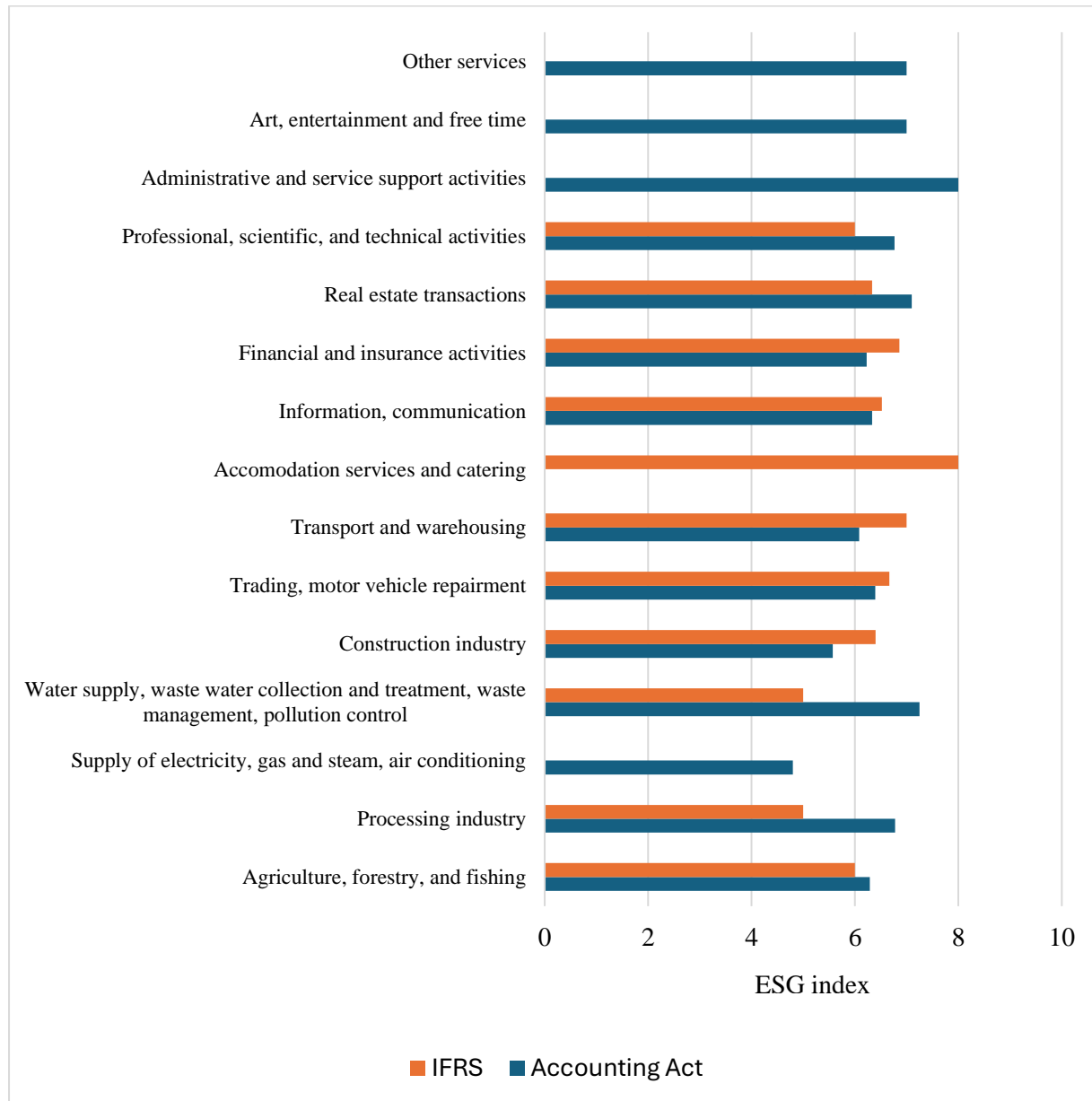
*Source: own editing, based on data provided by Hungarian Central Statistical Office.*

**Table No. 3**  
**Number of companies submitting consolidated financial statements and data on employment, 2021**

<b>Name of the sector</b>	<b>Number of companies (pcs)</b>	<b>Average number of employees in the current business year (person)</b>
Financial and insurance activities	48	31272
Professional, scientific, and technical activities	31	19680
Trading, motor vehicle repairment	30	14802
Processing industry	20	13534
Real estate transactions	17	7087
Transport and warehousing	14	100965
Construction industry	11	6103
Agriculture, forestry, and fishing	6	6275
Supply of electricity, gas and steam, air conditioning	4	2152
Information, communication	4	5930
Administrative and service support activities	4	12354
Water supply, waste water collection and treatment, waste management, pollution control	3	2760

*Source: own editing, based on data provided by Hungarian Central Statistical Office.*

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**Figure 1**  
**Averages of the ESG index by national economic sectors, 2022**  
*Source: own editing, based on data provided by Opten Ltd. (2024)*