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Accounting Profession in Italy; Professional Accounting in Foreign Country Series

Arthur Young International

Susan Sgromo

The Accounting Profession in Italy

PROFESSIONAL ACCOUNTING IN FOREIGN COUNTRIES SERIES

AICPA

American Institute of Certified Public Accountants

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Prepared by

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NOTICE TO READERS

The Professional Accounting in Foreign Countries series is designed to be educational and used as reference material for the members of the Institute and others interested in the subject. It is not intended to establish standards.

The International Practice Committee gratefully acknowledges the contributions made to the development of this series by former committee chairman Harvey D. Moskowitz; former committee members Dale D. Baker, R. Harry Beattie, Campbell E. Corfe, Perry D. Harbour, Walter F. O'Connor, W.C. Brian Peoples, Bruce D. Robertson, Martin Rotheim, and Gary S. Schieneman; and former staff aide James F. Flynn. The committee would also like to acknowledge the fine editorial efforts of Glenn Shephard and Carrie Vaccaro and the production work of Robert DiCorcia, Paul Smolenski, and Mary Hendrickson.

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Preface

This booklet is one of a series on professional accounting in foreign countries. The material is current as of July 1987. Changes after this date in the standards of either the United States or Italy may alter the comparisons detailed in this publication.

Included are descriptions of the accounting profession, auditing standards, and accounting principles in Italy. The booklet also presents brief descriptions of the various forms of business organizations, taxes, and requirements for stock exchange listings and securities offerings. Checklists comparing Italian auditing standards and accounting principles with those generally accepted in the United States are appendixes to the text.

This booklet is not intended to be a comprehensive discussion of auditing standards and accounting principles in Italy but is designed instead to focus primarily on differences from those of the United States.

John Graves
Director
Technical Information Division

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The Accounting Profession

REQUIREMENTS FOR ENTRY INTO THE PROFESSION

Domestic Functions and Licensing Requirements

1. Two types of professional accountants are recognized in Italy: the Dottore Commercialista (doctor of commerce) and the Ragioniere Collegiato (accountant and commercial expert). The activities of these two groups, which are governed by two separate laws enacted in 1953, are basically quite similar, the main differences relating to the educational and professional background of their members. (See paragraphs 12 through 14 for a discussion of the differences.)

2. The entire framework of business regulation in Italy is currently undergoing profound and rapid change. Traditionally accounts in Italy were prepared for tax purposes only, and formal auditing and accounting standards were unknown. There are still fewer than two hundred publicly listed companies on the Milan Stock Exchange (the largest stock exchange in Italy), and there has been little pressure from shareholder groups to improve auditing and reporting standards. Although both types of limited companies—the *Società per Azioni*, or S.p.A. (corporation), and the *Società a responsabilità limitata*, or S.r.l. (limited-liability company) with capital in excess of 100 million lire—have to appoint a Collegio Sindacale (board of statutory auditors), the work of the statutory auditors is little more than a formality.

3. To improve public confidence in corporate reporting, and to stimulate investment, a new stock exchange regulatory authority,

the Commissione Nazionale per le Società e la Borsa, or Consob, was established in 1974. Auditing requirements for listed companies, introduced by legislation that was enacted in 1975, became effective in 1982. These requirements were extended by subsequent legislation to other kinds of companies and certain state-owned enterprises. For insurance companies, a new supervisory authority similar to Consob, the Istituto per la Vigilanza sulle Assicurazioni Private e di Interesse Collettivo, or ISVAP, was established by a 1982 law that became effective in 1983.

4. Consob has recommended a number of new financial reporting and auditing standards issued by the profession, including the requirement for presenting consolidated accounts. Under the present Consob rules, audits can be performed by approximately thirty approved audit firms whose quality control and independence are monitored on a regular basis. One of the conditions for an audit firm to be included on the Consob list is that the majority of its partners or directors must be either Dottori Commercialisti or Ragionieri Collegiati with at least five years of audit experience. (Alternatively, they may qualify by passing a special Consob examination.) A Consob audit must comply with standards comparable to those recognized internationally. The auditor reports that the financial statements examined conform to the requirements of Italian commercial law and are in accordance with accepted accounting principles.

5. The Consob-approved audit firms established an association known as Assirevi to represent their interests and to improve professional standards.

6. New audit requirements are expected when the Fourth Directive of the European Economic Community (EEC) is adopted. There is no indication at present whether audits under these new requirements will continue to be limited to the Consob-approved audit firms or whether individual auditors will be recognized.

Foreign Reciprocity

7. Accountants from foreign countries that grant reciprocal treatment to Italian accountants may have their foreign degrees or diplomas recognized as being equivalent to Italian credentials.

Auditing qualifications and audit experience acquired in such countries may also be recognized as equivalent in Italy.

ROLES AND RESPONSIBILITIES OF STANDARD-SETTING BODIES

Professional Standards Promulgated by Each Body

8. In 1976 the Ordine Nazionale dei Dottori Commercialisti established two national commissions to develop proposed accounting and auditing standards for financial statement presentation and audits thereof. The Collegio dei Ragionieri e Periti Commerciali, which had initially formed its own commission, decided in 1983 to join in the Dottori Commercialisti's efforts. The standard-setting procedure initially proposed by these commissions was later modified, particularly with respect to accounting standards, to gain more general acceptance. In 1982, Consob decided to enforce the auditing standards issued by the Ordine Nazionale dei Dottori Commercialisti and recommended that the commissions' proposed accounting standards be observed (with some exceptions, still under study, relating to audit reports and financial statement presentation).

9. The accounting standards are intended to complement the basic principles set forth in the Italian Civil Code. At present, however, they derive their validity not from the law but from general acceptance, as evidenced by the recognition of Consob, the accounting profession, Assirevi, and other institutions. The auditing standards have been enforced as law under the terms provided by a Consob pronouncement of 1982; they are legally binding on the auditing firms, and are recognized as such by Assirevi.

Ethics Requirements

10. The rules of association of the Ordine Nazionale dei Dottori Commercialisti and of the Collegio Nazionale dei Ragionieri include some specific ethics requirements relating to the exercise of the profession of Dottore Commercialista or Ragioniere Collegiato. These requirements have to do with the auditor's independence and professional competence.

11. Auditing Standard No. 1 of the Consiglio Nazionale dei Dottori Commercialisti, *General Concepts Relative to Auditing Standards,* specifies the following ethics requirements for the auditor:

- Competence as a condition for acceptance of the auditor's work
- Exercise of due professional care in the conduct of the audit
- Integrity
- Independence

PROFESSIONAL PUBLIC ACCOUNTING ORGANIZATIONS

Requirements for Membership

12. Under current law, the practice of public accounting is limited to the professions of Dottore Commercialista and Ragioniere Collegiato. Little distinction is made between the professional activities of the Dottore Commercialista and the Ragioniere Collegiato: both can participate in the administration of business enterprises, appraisals, surveys, liquidation proceedings, administrative inspections, accounting verifications and audits, tax advice, and representation of clients before the tax authorities.

13. The designation *Ragioniere Collegiato* may be obtained through admission to membership in the Collegio dei Ragionieri e Periti Commerciali by graduates of a five-year business secondary school who pass a national examination dealing with the provisions and procedures of the Civil Code and with tax and accounting problems. Two years' practical experience in the office of a Ragioniere Collegiato or a Dottore Commercialista in public practice is required for admission to the state examination.

14. The designation *Dottore Commercialista* may be obtained through admission to membership in the Ordine dei Dottori Commercialisti by graduates of a four-year university course leading to the degree of Dottore in Scienze Economiche e Commerciali (doctor of economic and commercial science) who have also passed a special state examination that may be taken immediately after obtaining the university degree. There is no requirement for practical experience.

15. The designation *Revisore Ufficiale dei Conti* (official auditor) may also be obtained by registration in the Ruolo dei Revisori Ufficiali dei Conti (official register of auditors). Such registration can be obtained by any person of Italian nationality who has served for at least five years as an active statutory auditor, as a director, as

an administrative or accounting officer, or in a similar capacity in a business enterprise with a capital stock of not less than 50 million lire. This experience requirement is reduced to three years or four years, respectively, for a Dottore Commercialista or a Ragioniere Collegiato of at least five years' standing. It is not necessary that the registrant have had professional experience in examining and reporting on financial statements, as is required, for example, in the United States and the United Kingdom.

16. As noted earlier, the present law requires that, in order for an audit firm to be included on the Consob list, a majority of its partners and directors must be Dottori Commercialisti or Ragionieri Collegiati with at least five years of audit experience (or, alternatively, to have passed the special Consob examination).

Rights of Membership

17. Rights deriving from membership in the Ordine Nazionale dei Dottori Commercialisti or in the Collegio Nazionale dei Ragionieri consist mainly of the right to vote in the elections of these groups' national and local representative bodies (Consiglio Nazionale dei Dottori Commercialisti, and Collegio Nazionale dei Ragionieri) and to participate in the professional activities of the organizations.

Number of Members

18. Members of the profession of Dottore Commercialista in Italy currently total around 3,500. Members of the profession of Ragioniere Collegiato total approximately 18,500.

CPE Requirements

19. There are no specific requirements regarding continuing professional education (CPE) under the rules of association of either the Ordine Nazionale dei Dottori Commercialisti or the Collegio Nazionale dei Ragionieri, although both organizations frequently conduct educational programs for their members.

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Auditing Requirements

STATUTORY AUDITING AND REPORTING REQUIREMENTS

Purpose of the Statutory Audit

20. Any corporation whose liabilities are limited by shares (*Società per Azioni*, or S.p.A.) must have a board of auditors (*Collegio Sindacale*), commonly referred to as "the statutory auditors," to monitor its management and to perform certain verification procedures on its annual financial statements. These include procedures designed to ensure that the financial statements are in compliance with the Civil Code. The board consists of three or five active members ("sindaci") plus two substitute members and is appointed by the shareholders for a three-year term. However, board members can be elected for additional terms. Any limited-liability partnership (*Società a responsabilità limitata*, or S.r.l.) must also appoint a board of auditors when the partnership capital exceeds 100 million lire. The purpose of the board of auditors is to help safeguard the interests of shareholders and creditors.

21. The statutory auditors must be individuals (as opposed to firms or other entities), and they are required to do the following:

a. Review the management of the business
b. Determine that the provisions of the Italian laws and the company's articles of association are being observed
c. Determine that the company's books and accounts are in order
d. Determine that the company's annual financial statements agree with its books and other records and that they have been prepared in conformity with the relevant provisions of the Civil Code and other governing legislation

22. No standard form of audit report is required by the Civil Code. The Code merely provides that the statutory auditors must identify, and provide justification for, any deviations from recognized accounting principles. In addition, the statutory auditors are specifically required to report on the following matters:

- The basis of valuation of shares and bonds
- The method used to account for prepaid and deferred expenses
- Accrued liabilities and deferred expenses
- The amounts of any provisions for depreciation, depletion, or amortization set aside in any asset category

23. The statutory auditors are personally liable for the accuracy and truthfulness of their statements and, with the directors, are jointly liable for the directors' actions or omissions whenever it can be shown that a loss could have been avoided if the auditors had performed their duties properly.

24. The official register of auditing companies (Albo delle Società di Revisione), along with the requirement that listed companies be audited by one of these companies, was established to increase investors' confidence in companies listed on the Italian stock exchanges and thereby contribute to the development of a larger and more active market for Italian companies' shares. The audit performed by such a registered audit firm does not substitute, however, for the examination performed by the board of statutory auditors, even though some procedures are the same.

25. Subsequent to the requirement for listed companies to have their annual financial statements audited, legislation was introduced for other types of organizations, especially companies whose activities are vested with a public interest. For such companies, the audit requirement was to provide an attest function on the reliability of the financial information.

Entities That Are Required to Be Audited

26. The entities currently required to be audited by one of the firms listed on the official register are as follows:

a. Companies traded on any of the ten Italian stock exchanges
b. Companies controlled directly or indirectly by the Ministry of State Investments

c. Insurance companies underwriting risks other than death
d. Companies taking advantage of certain export schemes
e. Publishing companies with annual revenues of more than 10 million lire or employing more than five journalists
f. Certain municipal enterprises and utilities
g. Certain types of banks
h. Mutual funds

Appointment and Qualifications of Auditors

27. Only those audit firms included in the official register of auditing companies are entitled to perform audits. Inclusion in the register is determined by Consob.

28. Appointment of auditors is by a board of directors' resolution proposing that shareholders appoint the audit firm; the shareholders have the final choice. The appointment is for a three-year term and is renewable for a maximum of two additional terms.

29. For companies listed on the stock exchanges and for all publishing companies, the selection of an audit firm from the official register is subject to ratification by Consob after the board of directors' resolution but prior to the shareholders' appointment. In reaching its decision, Consob examines the audit proposal submitted by the audit firm, including audit time, experience, levels of personnel assigned, and estimated fees.

Auditing and Reporting Responsibilities

30. The auditor's responsibility is to report on the annual financial statements prepared by the directors for submission at the annual shareholders' meeting. The auditor's report must be available at the company's registered office fifteen days before the shareholders' meeting.

31. In addition to reporting on the annual financial statements, the auditor must record in the audit book ("libro della revisione") the principal audit procedures performed and the findings and conclusions. In this book, which is available for inspection by tax and judicial authorities, by the company's board of directors, and

by its board of statutory auditors (but not by its shareholders), the auditor records the major auditing procedures performed, the opinion given on the financial statements under examination, and, eventually, any irregularities or illegal acts noted during the course of the examination.

32. The audit firm does not have any direct responsibility to the tax authorities, whereas the chairman of the board of statutory auditors is required to countersign the company's tax return.

33. The report of the registered audit firm must explain the procedures and test checks carried out, and must certify that the balance sheet and the profit and loss statement agree with the company's books, have been prepared in the prescribed form, and fairly reflect the operations of the business in conformity with recognized accounting principles. If the audit firm deems itself not to be in a position to provide such certification, it must explain the reasons therefor in its report and inform Consob immediately.

34. The audit firm is required to be independent of the company it audits. Its personnel must carry out all work that they consider necessary to enable them to fulfill their duties as auditors; they may not accept any restrictions relating to such work.

35. There is no legal or governmental requirement for private (that is, unlisted) companies to be examined by independent auditors.

Filing of Reports

36. The auditor's report on the official annual financial statements is addressed to the stockholders and is presented at the annual general meeting. As mentioned above, the report must be available fifteen days before the shareholders' meeting.

37. If the company has a controlling interest in any subsidiaries, it is required to prepare consolidated financial statements, and an additional auditor's report must be issued on the consolidated statements. However, such consolidated statements may be prepared up to six months after the date of approval of the official financial statements.

SUMMARY OF SIGNIFICANT AUDITING STANDARDS AND COMPARISON WITH U.S. GENERALLY ACCEPTED AUDITING STANDARDS (GAAS)

Standards Issued

38. In 1981, Assirevi resolved to approve and adopt all the existing auditing standards established by the Dottori Commercialisti. To date, out of eighteen established auditing standards, seventeen have been approved by Assirevi. Auditing Standard No. 18, *The Auditor's Opinion,* has not been formally approved by Assirevi since, as soon as it was issued, Consob issued its own recommendation for the auditor's report, which contains language that is significantly different from the language recommended by the Dottori Commercialisti. Consob has also approved (with the exception of No. 18) the auditing standards established by the Dottori Commercialisti. (See appendix A for a list of auditing standards.)

39. In addition, standards on the following subjects are being developed by the profession:

a. Irregularities and illegal acts
b. Related-party transactions
c. Auditing standards for banks and insurance companies
d. Auditing standards for investment companies

40. From time to time, Assirevi issues recommendations to its members to promote uniformity among accounting firms with regard to auditing practices that are not covered by a standard issued by the profession.

41. There are no significant differences between Italian and U.S. auditing standards and procedures. (See appendix D for a summary comparison of U.S. and Italian auditing standards.)

General Standards

42. In general, Italian standards are similar to U.S. standards. Briefly, they are as follows:

a. The auditor is required to have and maintain, through constant training, an adequate level of competence.

b. Due professional care is to be exercised when performing an audit.

c. The auditor must be independent in both fact and appearance.

d. No auditor may engage in advertising of any kind.

e. Auditors must maintain good relations and cooperate with one another. (An auditor may use another auditor's services.)

f. Services provided are to be adequately compensated.

43. As far as the auditor's responsibility is concerned, the standard provides that the auditor is legally and professionally liable only when he or she fails to apply, or incorrectly applies, the required auditing standards. The auditor cannot be considered responsible for failure to detect fraud or illegal acts if the audit procedures appropriate in the circumstances have been competently performed.

44. With regard to independence, the law sets forth stringent rules and concludes by requiring that the auditor keep himself or herself at all times in such a position as never to impair his or her independence in relation to the company.

Standards of Fieldwork

45. There are no significant differences between Italian standards of fieldwork and U.S. standards, that is—

a. The audit is to be adequately planned.

b. The auditor must study and evaluate the internal control system. Should the auditor decide to rely on the company's internal controls, the nature and extent of the auditing procedures are to be determined accordingly.

c. The auditor must examine sufficient competent evidential matter to substantiate his or her professional opinion.

d. Sampling plans must provide assurance that the samples drawn are representative of the entire universe tested.

Standards of Reporting

46. As noted earlier, Auditing Standard No. 18 has not been accepted by Consob and has not been approved by Assirevi. Auditing

Standard No. 18 states that, as recommended by Accounting Principle No. 2, *Form and Presentation of Financial Statements for Manufacturing and Sales Companies*, the financial statements of an Italian company are intended to comprise the following items:

a. Statutory balance sheet
b. Statutory income statement
c. Reclassified balance sheet (in order of liquidity)
d. Reclassified income statement (in a form similar to that used in the United States)
e. Statement of changes in financial position
f. Statement of changes in equity accounts
g. Notes to the financial statements

47. Both Consob and Assirevi have agreed that a set of financial statements should include the above items. In 1983, however, in issuing its recommendation on the language of the auditor's report, Consob drastically changed the format proposed by the profession, making it much more legalistic in form (see appendix C). The auditor's report called for by Consob consists of four main paragraphs, as follows.

a. The first paragraph deals with the identification of the financial statements on which the audit firm is reporting and with the formal engagement to perform such an examination.
b. The second paragraph includes what in the United States is called the scope paragraph, and also mentions—
   - The source of the accounting principles used.
   - The parts of the directors' report that are necessary for a clear understanding of the financial statements. (In the United States such information is provided in notes to the financial statements.)
   - Any other information with which the accountant is directly associated or in connection with which the accountant wants to limit his or her responsibility.
   - Reference to the previous year's report, if any. (Contrary to common practice in the United States, the officially prescribed auditor's report in Italy does not require reporting on comparative statements, although such reporting is recommended.)

c. The third paragraph is used for comments on any significant matters relating to the financial statements under examination that the auditor believes should be brought to the reader's attention. The third paragraph is also used to identify any deviations from generally accepted accounting principles that do not materially impair the clarity and fairness of the financial statements. Any uncertainties and any instances of the use of accounting methods in accordance with the tax rules (instead of generally accepted accounting principles) to secure tax benefits that would not otherwise be available are also pointed out in this paragraph.

d. The fourth and final paragraph is the opinion paragraph, in which the auditor attests that (1) the financial statements agree with the transactions recorded in the accounting records and with the results of the auditing procedures performed; (2) the statements conform to the Civil Code's requirements for the presentation and content of financial statements; and (3) the accounting principles used to record the business transactions are correct. As opposed to U.S. practice, the consistency standard is implied but not written, unless an inconsistency is noted.

48. The auditor's report must be signed individually by the partners in the audit firm who are responsible for the engagement.

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Accounting Principles and Practices

SOURCES OF ACCOUNTING PRINCIPLES

49. The Civil Code prescribes the contents of the financial statements and the basic principles for valuing assets and liabilities. In addition, rules of valuation are frequently enforced through tax regulations. Detailed accounting principles derive from a series of statements issued in recent years by the accounting profession. (See appendix B for a list of accounting principles.) The Civil Code, which is complemented by these statements of accounting principles, refers to the fundamental principles of consistent application of accounting policies, prudence, the accrual concept, and historical cost as the basic valuation criteria.

50. Special rules are in force for certain enterprises, such as insurance companies, banks, investment funds, publishing companies, and utilities.

FORM AND CONTENT OF FINANCIAL STATEMENTS

Presentation of Statements

51. The Civil Code requires that a balance sheet and a statement of revenues and costs be prepared. The balance sheet follows the traditional form, with assets on the left side and liabilities on the right side, whereas the statement of revenues and costs shows revenues on the left side and costs on the right side. (See appendix

C for illustrative examples.) The offsetting of accounts is not permitted. For example, the gross book value of fixed assets is shown on the left side of the balance sheet and accumulated depreciation on the right side.

52. The Dottori Commercialisti pronouncements provide more specific guidance, calling for—

a. A reclassified balance sheet that classifies assets and liabilities as current versus long-term, shows the working capital and equity position of the company, and nets contra asset accounts, such as accumulated depreciation and allowance for doubtful accounts, against the related assets. (This information is not readily determined from the statutory financial statements.)
b. A reclassified income statement that shows gross profit, operating income, pre-tax income, and extraordinary items. (This information, too, is not readily identifiable in the statutory financial statement.)
c. A statement of shareholders' equity.
d. A statement of changes in financial position.

53. The above-described additional financial information cannot yet be considered to be generally accepted. In fact, small and medium-sized Italian companies frequently file only the financial statements specifically called for by the Civil Code.

54. The directors of a company are required to submit a directors' report and the financial statements (audited by the statutory auditors and, if required, by an independent accounting firm) to the shareholders for their approval at the annual general meeting, which in normal circumstances takes place within four months after the company's year-end date. Such statements must then be filed with the courts and with the tax authorities. For a listed company, the directors must publish an interim (semiannual) unaudited report on the activities of the company within three months after the applicable six-month period.

55. The annual directors' report presents the directors' views on the company's operations. The following matters are to be disclosed in the directors' report:

a. Principal activities and discussion of the business of the company (and subsidiaries) during the year

b. Important events that occurred after the year end and affect the company
c. Accounting principles followed, and any changes from the accounting principles followed in the previous year
d. Analyses of and comments on variations in the asset and liability accounts as compared with the previous year
e. Information on personnel matters
f. Interest expense on short- and long-term borrowing
g. Intangible assets capitalized during the year (such as research and development, advertising, and start-up costs)
h. Major transactions with the parent company or subsidiaries
i. Guarantees granted and obtained
j. Information on long-term debts
k. Contingent assets and liabilities
l. Recommended dividend distribution

56. If special reasons make it necessary to depart from the bases of valuation prescribed by the Civil Code, the directors and the board of statutory auditors are required to state such reasons and to justify each individual case when reporting to the shareholders on the accounts.

57. All companies, except S.r.l.'s with a capitalization of less than 100 million lire, are required by the Civil Code to appoint a board of statutory auditors. The statutory auditors must issue their report on the financial statements presented for approval by the shareholders at least fifteen days before the annual shareholders' meeting.

58. In addition, certain entities (for example, listed companies, insurance companies, state-owned companies, firms, and investment publishing companies) are required to appoint an independent accounting firm, which also must issue an audit report at least fifteen days before the financial statements are approved by the shareholders.

Types of Statements Prepared

59. A listed company with subsidiaries may be required by Consob to publish, in addition to the parent company's financial

statements, consolidated financial statements within six months after its year-end date. Although the current rules do not call for audited consolidated financial statements, it is nonetheless common practice to have them audited by an independent accounting firm. It is also becoming common practice for unlisted companies to publish consolidated statements.

60. The Civil Code prescribes that, in the case of a group, the financial statements of the parent company must include, as an attachment, a copy of the latest approved financial statements of its subsidiaries, as well as condensed information on companies in which a minority interest is held.

61. As noted earlier, special rules, calling for different forms of financial statements, apply to companies in certain industries.

62. The Civil Code, as revised in 1974, prescribes standard formats for the balance sheet and the profit and loss statement. The balance sheet follows the traditional form, with assets on the left side and liabilities on the right side. The Civil Code requires that items be classified under the following headings.

*Assets**

- Stock subscriptions owed by shareholders
- Land and buildings
- Machinery and equipment
- Furniture and fixtures
- Patents and copyrights
- Trademarks and goodwill
- Inventories of raw materials and merchandise
- Cash on hand
- Cash in banks
- Bonds
- Marketable securities
- Long-term investments
- Treasury stock

*Although not mentioned in this classification, prepaid and deferred expenses are usually shown separately, with an appropriate description. The Civil Code recognizes the principle of allocating certain costs over a period of more than one year.

- Accounts receivable from customers
- Accounts receivable from affiliated companies
- Other receivables
- Memorandum accounts (per contra)

Liabilities

- Capital stock
- Statutory (legal) reserve
- Other reserves
- Accumulated depreciation and amortization
- Accrued severance indemnities
- Liabilities for which collateral or other security has been given
- Trade accounts payable
- Amounts owing to bankers and other lenders
- Amounts owing to affiliated companies
- Bonds issued
- Other liabilities
- Memorandum account (per contra)

63. The offsetting of accounts in the balance sheet is not permitted. Notes to the financial statements, such as disclosures of liabilities and material lease commitments, are rarely included.

64. As revised in 1974, the Civil Code prescribes that the profit and loss statement include all revenues and expenses of the period, classified as follows.

Revenues

- Sales and services by category
- Property investment income
- Dividends from subsidiaries and affiliated companies
- Dividends from other investments
- Interest income on fixed-income securities
- Interest income on bank accounts
- Interest income on receivables from subsidiaries and affiliated companies
- Interest income on accounts receivable
- Interest income on other receivables
- Gains from disposal of assets

- Additions to plant, equipment, and other assets by internal construction
- Other income, revenues, and gains
- Closing inventory of raw materials, work in process, and finished products

Expenses

- Opening inventory of raw materials, work in process, and finished products
- Purchases of raw materials, work in process, and finished products
- Labor and social-contribution costs
- Costs of services received
- Income and other taxes, showing separately those relating to prior years
- Interest charges on bonds
- Interest expense on accounts payable to subsidiaries and affiliated companies
- Interest expense on bank accounts
- Interest expense on other payables
- Discounts and other financial charges
- Depreciation provision in each fixed-asset category
- Provision for employee severance payments, pensions, etc.
- Provision for devaluation of marketable securities and other assets
- Provision for bad debts
- Losses on devaluation of assets
- Other expenses and losses

65. The offsetting of accounts in the profit and loss statement is prohibited. There is no requirement in the Civil Code to provide a statement of changes in financial position.

66. The Civil Code contains no requirement to prepare consolidated statements, but it requires that annual accounts include a supporting schedule listing any holdings in subsidiaries or associated companies and disclosing the nominal and carrying values of each such holding. A subsidiary is defined as any entity in which a majority of the voting rights is owned; an associated company is

defined as any company in which 10 percent of the shares is owned. A complete set of the most recent annual accounts of each subsidiary company must be attached to the parent company's own accounts. Key financial information, including turnover and results for the period, must also be given for each associated company.

67. Although the Civil Code does not require consolidated financial statements, Consob has required them from virtually all listed companies since 1982. Prompted by Consob's action, the accounting profession has given a high priority to the development of standards for the preparation of consolidated statements. A standard on consolidation has been issued but not yet officially approved.

SUMMARY OF SIGNIFICANT ITALIAN ACCOUNTING PRINCIPLES AND COMPARISON WITH U.S. GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (GAAP)

Accrual Basis

68. The accrual basis of accounting is the only acceptable basis for financial statements prepared in accordance with the Civil Code.

Consolidation

69. The concept of consolidation is not mentioned in the Civil Code, and as a result it is not common for consolidated accounts to be prepared by unlisted companies in Italy. Instead, the separate accounts of majority-owned subsidiaries are commonly attached to those of the parent company. For other associated companies that are at least 20 percent owned, only certain basic data, such as sales, total assets, and net income, are disclosed.

70. A recently enacted law provides for Consob, at its discretion, to require companies listed on the stock exchange to present consolidated financial statements. Consob has already imposed this requirement on all listed companies. The state-owned enterprises have also followed Consob's recommendations and are now presenting consolidated statements.

Deferred Tax Accounting

71. As a general rule, expenses deductible for tax purposes in Italy must be reflected in a company's financial statements. For example, for a company to be able to take advantage of accelerated depreciation for tax purposes, accelerated depreciation must be used for financial reporting purposes. Certain expenses, however, are subject to maximum allowable percentages that may be different from amounts recorded in the financial statements under the tax rules. In connection with doubtful accounts, for example, the Civil Code requires that receivables be stated at net realizable value, thus requiring estimation of an appropriate provision for doubtful accounts, whereas the tax laws permit only a certain percentage of total receivables to be tax-deductible in any given year. Similarly, repair and maintenance expenses are tax-deductible in any given year only up to a maximum of 5 percent of total fixed assets.

72. Deferred tax accounting for such book/tax timing differences is not prescribed by the Civil Code and is not generally practiced by privately owned companies.

73. By virtue of their endorsement of the international accounting standards, the Dottori Commercialisti have implied that the practice of deferred tax accounting should be followed. It should be noted, however, that under the existing tax laws, book/tax timing differences generally result in prepaid taxes. Italian companies are reluctant to record such deferred tax debits.

Revenue and Expense Recognition

74. Under the Civil Code, as a general rule, revenues are to be recognized only when their realization is at least reasonably certain and objectively measurable, whereas expenses are to be accounted for when they are expected to be incurred. In the past, observance of this rule has caused problems, since expenses are deductible for tax purposes only when they are incurred. However, business practices are gradually leading toward a revision of the tax laws in this regard.

75. The pronouncements of the Dottori Commercialisti clearly indicate that the tax rules are not an acceptable alternative to recognized accounting principles in the preparation of financial statements.

Noncurrent Assets

76. Fixed assets must be depreciated on a systematic basis, according to their residual estimated useful lives. The method used to depreciate fixed assets may be determined in accordance with the specific circumstances, but in practice the straight-line method is by far the most commonly used. Intangible assets are recognized as such only when a cost has actually been incurred to acquire them and a future benefit is expected. Amortization generally is provided on a straight-line basis over a period of five years. The Civil Code provides that certain intangible assets can be amortized over a longer period.

Inventory

77. Under the Civil Code, inventories must be valued using the lower-of-cost-or-market method. The LIFO method of determining inventory cost, which is the method required for tax purposes, generally is used for financial statement purposes.

78. The Dottori Commercialisti have provided definitions of the various types of costs that can be capitalized in inventories and the methods acceptable for their valuation. Generally speaking, all costs that contribute, directly or indirectly, to the physical formation of the inventory may be capitalized, whereas selling, administrative, and financial expenses may not.

Long-Term Contracts

79. The accounting for contracts whose execution requires more than one year is not dealt with by the Civil Code. Most commonly, the percentage-of-completion method is used, although the completed-contract method is an acceptable alternative. A pronouncement on this subject from the Dottori Commercialisti is pending. Losses on long-term contracts normally are recognized as soon as they are known.

Investments

80. Investments generally are carried at cost. Because of tax regulations that take equity adjustments into taxable income, equity accounting is not generally practiced in Italy except when the investee has incurred operating losses. The effect of applying the

equity method is disclosed, however, in the notes to the financial statements or in the directors' report.

Foreign Currency Translation

81. The Civil Code does not specifically deal with accounting for exchange gains and losses on foreign currency transactions. The predominant practice is to use the current rate if translation results in a loss and the historical rate if translation results in a gain. It should be noted that, for tax purposes, unrealized exchange losses are not deductible but recorded exchange gains are taxable.

82. With respect to the translation of foreign subsidiaries' financial statements, the balance sheet and income statement generally are translated at year-end exchange rates. Translation adjustments are included as part of shareholders' equity.

Leasing

83. The existing legislation does not prescribe any accounting treatment for leases, either for lessors or for lessees. The current practice is to use the operating method for all long-term leases.

84. Although the finance method of accounting is not presently used by lessors in Italy, many companies disclose the effect of its application in notes to the financial statements or in the directors' report.

Acquisitions and Mergers

85. The only accounting method allowed by Italian law for acquisitions and mergers is the purchase method.

Goodwill

86. Italian companies may record goodwill only if it has been purchased as part of a business acquisition. Goodwill is capitalized and amortized over its estimated useful economic life. In practice, goodwill is the difference between the purchase price and the value of identifiable assets as agreed by the parties. Fair value accounting is not required for assets obtained in an acquisition.

Income Taxes

87. Loss carrybacks are not permitted by law, while losses are allowed to be carried forward and offset against income (for purposes of the national income tax only) for five years. Loss carryforward benefits are not segregated as extraordinary items when realized, and neither their availability nor their expiration date is ordinarily disclosed in Italian financial statements.

Accounting Changes

88. All accounting changes are handled on a prospective basis. The effects of such changes must be disclosed in the financial statements. No retroactive adjustments are permitted. Corrections of errors are charged or credited to income in the year of recognition.

Inflation Accounting

89. There is no requirement that Italian companies submit information on the effects of inflation.

Other Matters

90. A number of accounting practices observed in the United States do not have a corresponding practice in Italy.* The most important of these follow.

- Interim financial reporting (not commonly practiced in Italy)
- Financial reporting for segments of a business enterprise
- Accounting by debtors and creditors for troubled-debt restructuring
- Prior-period adjustments
- Accounting for forward exchange contracts
- Financial reporting and changing prices
- Pensions (no consideration is ordinarily given to discounted schemes)

*Appendix E contains a summary comparison of U.S. and Italian accounting principles.

4

Business Environment

FORMS OF BUSINESS ORGANIZATION

Entities With Corporate Attributes

Comparison With U.S. Entities

91. The Italian form of business organization that most closely resembles a U.S. corporation is the joint stock company, or *Società per Azioni* (S.p.A.). This type of corporate entity must have a minimum capital of 200 million lire and, in order to maintain its limited-liability status, more than one shareholder. The capital may be in kind, in which case it is subject to various valuation and appraisal procedures. Should the capital stock be greater than 10 billion lire, its issuance is subject to approval by the Treasury Department.

92. Other types of Italian entities with corporate attributes are—

a. *The Società in accomandita per Azioni,* or S.a.p.A., which is a special form of partnership whose general partners are shareholders and directors and are liable for the partnership's obligations jointly and severally. This type of business organization is not as commonly encountered as it once was.

b. *The Società a responsabilità limitata,* or S.r.l., which is similar to a limited-liability partnership in which the liability to third parties is limited to the extent of the company's assets. The capital cannot be represented by shares but may be divided into quotas or parts. The required minimum capital is 20 million lire.

93. An S.p.A. or S.r.l. must hold a general meeting at least once a year. In addition, a shareholders' meeting must be held when

amendments are to be made to the entity's bylaws or when directors and auditors are to be elected.

94. Shareholders of an S.p.A. or an S.r.l. are liable only to the extent of their capital contributions, except that, should there be only one shareholder at any time, such shareholder is liable, without limitation, for all obligations of the company arising during the period in which he or she is the sole shareholder.

95. Promoters, on the other hand, are liable jointly and severally to third parties, principally for—

a. The complete subscription of the company's capital and the payments required for the formation of the company.

b. The physical or ascertained existence of all contributions in kind.

c. Any misstatements of information disclosed to the public in connection with the formation of the company.

The promoters have no recourse against the subscribers of shares if the company is not formed.

96. The company's management may be entrusted to a single director or to a board of directors. Directors have an obligation to perform the duties set forth in the company's bylaws, as well as those in Italian company law, and may be held liable for damages deriving from failure to perform such duties. In addition, directors are liable jointly and severally should they fail to supervise the general conduct of the company's affairs or if, being aware of prejudicial acts, they did not try to prevent their occurrence or to eliminate or mitigate their harmful consequences. Directors are also liable to the company's creditors for failure to perform their duties relating to the preservation of the company's assets.

97. The Civil Code provides that corporations must have a board of auditors to supervise the management of the company, to verify the regular keeping of the company's accounts and their compliance with the provisions of the law, and, in general, to safeguard the interests of the shareholders. Statutory auditors are liable, along with the directors, for the latter's conduct when injury to third parties would not have occurred had the statutory auditors properly fulfilled their duties.

98. An amount equal to 5 percent of the company's (S.p.A. or S.r.l.) after-tax profit each year must be placed in a statutory reserve until such reserve equals 20 percent of the company's paid-in capital.

Branch of a Foreign Company

99. Foreign companies with one or more branches permanently established in Italy are subject to the provisions of Italian law regarding the filing and registration of the company's governing statutes, submission of the company's financial statements to the courts as though the branch were a separate legal entity, publication of the names of persons representing the branch on a permanent basis in Italy, and so forth. Although considered an independent entity for the fulfillment of certain tax and other official requirements, the branch is not in fact a legal entity in itself, so that foreign corporations establishing branches in Italy are liable for the acts and obligations of such branches.

Partnership Entities

100. There are several types of partnership entities in Italy that closely resemble U.S. partnerships. The two principal partnership entities are—

a. *The Società in nome collettivo* (S.n.c.), a general partnership in which all partners are liable without limit for the partnership's obligations.

b. *The Società in accomandita semplice* (S.a.s), a partnership in which there exist general partners who are liable without limit and limited or silent partners whose liability is restricted to the amount of their contribution to the firm's capital. Should the silent partners take active roles in the management of the partnership's business, their liability becomes unlimited.

Other Forms of Business Organization

Sole Proprietorship

101. The Italian form of sole proprietorship is similar to its counterpart in the United States.

Family Enterprise

102. A special type of business organization is the recently established "family enterprise," which may be formed through a notarized agreement made by members of a family participating in a business activity and in the sharing of the profits therefrom in accordance with an understanding reached among them. Important business decisions, including the decision to dissolve the enterprise, require a majority vote of the participating family members.

Other

103. Other common types of business enterprise include cooperatives and mutual insurance companies, which may have either unlimited or limited liability.

REQUIREMENTS FOR PUBLIC SALES OF SECURITIES AND REQUIREMENTS FOR LISTING SECURITIES ON STOCK EXCHANGES

Registration Requirements for Public Sale

104. An offer to sell or underwrite new securities (shares or bonds) must be communicated to the Italian securities regulatory agency, Consob, indicating the quantities and characteristics of the securities offered. All public offerings must be accompanied by a prospectus, including a description of the company (for example, history, capital stock, board of directors, and statutory auditors), its financial statements, trends of the business, and other information. Within twenty days of the date of application, Consob may request other data necessary to provide a complete picture of the offering to the public.

Requirements for Listing Securities on Major Stock Exchanges

105. There are ten Italian cities with stock exchanges: Bologna, Florence, Genoa, Milan, Naples, Palermo, Rome, Trieste, Turin, and Venice. The requirements for listing securities on the ten exchanges are essentially the same. The most important requirements, which are in accordance with EEC Directive 79/279, follow.

a. For the company*—
- Net equity is to be at least 10 billion lire for banks and at least 50 billion lire for insurance companies.
- The applying company must show profitable financial statements for the past three years.
- The financial statements of the last financial year must have been audited by a qualified accounting firm.

b. For its shares—
- Shares must be freely transferable.
- At least 25 percent of the shares must be distributed to the public. (Very few exceptions to this rule are permitted.)

c. For its bonds—
- The minimum amount of a bond issue is 10 billion lire, and at least 25 percent of the bonds must be distributed to the public.

106. The publication of a prospectus with the same contents as described in paragraph 104 for the public sale of securities is required before share or bond issues are negotiated.

107. Public companies must furnish Consob with, or notify it of, the following:

a. Annual financial statements
b. Proposals for changes in the company's bylaws
c. Shareholders' meetings
d. A report on business trends of the first six months, with particular attention to production, sales, and services
e. Interim dividends
f. Investments of over 2 percent in public companies or over 10 percent in nonpublic companies
g. Any investments in the company or in other companies of the same group by its directors, statutory auditors, or managing directors
h. Any other data requested

*In certain unusual cases, Consob may accept for listing a company with a net equity less than the required amount or with profitable results for less than three years, or it may permit the audit report for the last financial year to cover the balance sheet only.

TAXES

Principal Types

108. The present Italian system of income taxation has been in effect since January 1, 1974. It should be noted that the tax rules are undergoing revision; it is expected that new rules will be in force starting in 1988.

109. Income taxes are levied on a national basis on individuals (IRPEF) and business entities of all kinds (IRPEG), as well as on a local basis (ILOR).

110. IRPEF is levied progressively at rates that increase with the taxpayer's level of income and that range from 18 percent to 62 percent. IRPEG is levied at a rate of 36 percent on business income from all sources. ILOR is a local income tax levied on certain individuals and business entities at a rate of 16.2 percent. ILOR is deductible from IRPEF or IRPEG taxable income, resulting in an effective income tax rate of 46.37 percent for companies.

111. Income tax is withheld, at fixed rates, from most payments of interest, dividends, and royalties, and such withholdings usually represent a final tax for individuals, whereas they are considered payments on account of income taxes for companies.

112. Income taxes apply to both resident companies, which are subject to tax on their worldwide income, and nonresident companies, which are subject to tax only on Italian-source income (that is, income deemed to have been produced in Italy).

113. The foreign tax credit granted under Italian law and the various treaties to which Italy is a party minimize the incidence of double taxation on foreign companies.

114. Dividends paid to resident companies, as defined by law, are subject to a withholding tax of 10 percent. Resident shareholders enjoy a tax credit for the IRPEG tax paid by the company that distributes the dividends, thus eliminating double taxation. Dividends paid to nonresident companies or individuals are subject to a final withholding tax of 32.4 percent unless existing tax treaties provide otherwise.

115. A recent law provides for an equalization tax of 15 percent on distributions of profits earned by a company through December 31, 1982. On distributions of income earned after that date, the equalization tax rate is 56.25 percent of the distributed amount in excess of 64 percent of the company's taxable income.

116. The Italian government offers investors in certain areas (principally the south of Italy, or the Mezzogiorno) several incentives, including tax holidays, cash grants, long-term loans at low interest rates, and reduced social insurance contributions. With respect to income taxes, the most common incentives are *(a)* exemption from national income tax for ten years from the date of the company's formation and *(b)* total exemption from the local income tax (ILOR) for ten years, beginning with the first year in which business income is produced.

117. Value-added tax (IVA) is levied at various rates, the most common of which is 18 percent. Other taxes are as follows:

- Local tax on the increase in value of immovables (INVIM)
- Registration tax
- Stamp duty
- Estate and gift tax
- Manufacturing tax on items such as spirits, petroleum products, and beer
- Social insurance contributions

Tax Returns

118. Income taxes are assessed and collected through tax offices located in each major municipality. The value-added tax and the registration tax are assessed and collected by different tax agents, who operate independently of the income tax authorities.

119. For income tax purposes, companies must file their tax return not later than one month after issuing their annual financial statements (usually four to six months after the end of their financial year). A set of financial statements must be included with the company's annual income tax return.

120. Advance payments of national and local income taxes (IRPEG and ILOR), to the extent of 92 percent of the tax paid in the

preceding year, are due in November of each year, with the balance payable at the time the tax return is filed.

121. The statute of limitations is five years unless a return has not been filed, in which case it is six years.

122. Tax assessments issued by the appropriate authorities may be subject to four levels of tax jurisdiction before settlement. It is obvious, in these circumstances, that the final settlement of tax liabilities in Italy is not quickly achieved. Tax losses may be carried forward for five years for national income tax purposes only. No carryback of losses is allowed.

123. Tax returns are prepared using forms that are issued every year by the Ministry of Finance. The following documents are to be filed with the annual tax return:

a. A copy of the report of the board of directors' meeting, with the directors' recommendations to the shareholders to approve the financial statements as prepared by them
b. A copy of the minutes of the shareholders' meeting approving the financial statements
c. A copy of the company's financial statements
d. A copy of the report of the board of statutory auditors on the company's financial statements
e. Supporting documentation relating to advance payments of national and local income taxes and to taxes withheld from dividends received

124. For tax purposes, taxable income is determined on the basis of the results shown in the official financial statements modified to reflect specific tax rules. The taxpayer is free to furnish analyses and detailed schedules supporting the amounts in the financial statements. It should be noted that, historically, companies in Italy have embodied in their financial statements certain of the requirements of the tax rules to avoid differences between pre-tax income of the year and taxable income, since Italian tax laws generally require that tax returns be based on a company's financial accounting records. Thus, costs and expenses not included in the compa-

ny's financial statements are not allowed as deductions for tax purposes.

125. The main tax rules governing the preparation of tax returns may be summarized as follows:

a. Costs and expenses are to be accounted for on the accrual basis.
b. Inventory is to be valued at cost by the LIFO method. (Interest charges and nonmanufacturing overhead are excluded.)
c. Interest paid on loans entered into for the purchase or construction of plant assets must be capitalized through the tax period prior to that in which such assets are used or could be used in the business.
d. Depreciation is to be computed using the straight-line method, at rates not exceeding those approved by the Ministry of Finance.
e. Accelerated depreciation, at the rate of 15 percent for the first three years from the date of acquisition or construction, is also allowed. In any given year, depreciation rates must not be less than 50 percent of the maximum allowable rates.
f. Intangible assets may be amortized at a maximum rate of 20 percent per annum.
g. Research and development costs may be expensed entirely or deferred at the rate of 20 percent to 50 percent from the year in which the cost is incurred.
h. Advertising expenses are fully deductible in the year in which such expenses are incurred.
i. Taxes other than national income tax generally are fully deductible.
j. Repairs and maintenance costs are deductible to the extent of 5 percent of the total balance of depreciable assets at the beginning of the year. Any excess is deductible in equal amounts in the next five tax periods.
k. Exchange losses are deductible only when realized. However, exchange gains, if recorded, are taxable even though not yet realized.
l. Capital gains realized from the sale or disposal of business assets are taxed at ordinary rates.
m. Intergroup transactions must be on an arm's-length basis.

OTHER MATTERS OF IMPORTANCE

New Issues of Stock or Mergers of Publicly Traded Companies

126. When a publicly traded company issues new capital stock, or when a public company is merged into another public company or acquires a new subsidiary, Consob imposes the following requirements: (*a*) The auditors must report on the fair value of the shares exchanged in a merger transaction and on the fair value of the issue price for new capital shares; (*b*) the directors of the company must prepare a report discussing the major features of the transaction; and (*c*) the auditors are required to evaluate the fairness of the appraised values attributed to the assets in establishing the price of the shares issued. Both the directors' and auditors' reports must be made available upon request to the shareholders.

Legal Audits

127. For audits performed in accordance with the law, the related documentation must be included in a special register, the Register of the Audit Process. The required documentation includes a detailed description of the audit procedures followed in examining the financial statements of the company, the results of the examination (including any errors or irregularities found), and a copy of the entire auditor's report.

APPENDIX A

Italian Auditing Standards

Of the eighteen auditing standards issued to date by the profession in Italy, seventeen have been officially approved by Consob. The eighteen standards, translated from the Italian, are listed below.

No. 1	*General Concepts Relative to Auditing Standards*
No. 2	*Ethics Rules*
No. 3	*General Standards*
No. 3.1	*Internal Control*
No. 3.2	*Internal Control in the EDP Environment*
No. 4	*Supporting Documentation*
No. 5	*Auditing Procedures for the Examination of Financial Statements: Introduction and Accounting Records*
No. 6	*Inventories*
No. 7	*Accounts Receivable*
No. 8	*Cash and Bank Accounts*
No. 9	*Property, Plant and Equipment and Related Depreciation*
No. 10	*Intangible Assets and Amortization*
No. 11	*Marketable Securities and Long-Term Investments*
No. 12	*Accounts Payable*
No. 13	*Accrued Liabilities*
No. 14	*Liability Reserves*
No. 15	*Equity Accounts*
No. 16	*Memo Accounts (Contingent Liabilities and Commitments)*
No. 17	*Auditing Procedures Relative to the Income Statement*
No. 18	*The Auditor's Opinion*

APPENDIX B

Accounting Statements Issued by the Accounting Profession in Italy

Statement No.	Title
0	*Presentation and Introduction*
1	*Financial Statement Objectives and Underlying Assumptions*
2	*Form and Presentation of Financial Statements for Manufacturing and Sales Companies*
2 bis	*Integration of Number 2*
3	*Inventories*
4	*Fixed Assets*
5	*Bank Deposits and Overdrafts*
6	*Receivables*
7	*Current Liabilities*
8	*Consolidated Financial Statements; Investments*

APPENDIX C

Illustrative Auditors' Report and Financial Statements

The following financial statements are taken from the 1984/1985 annual report of Perugina S.p.A. The statements presented are not intended to include all information that Italian law requires.

AUDIT REPORT AS REQUIRED BY ART. 4 OF D.P.R. NO. 136 DATED MARCH 31, 1975*

To the Shareholders of
Perugina S.p.A.

1. In order to fulfill the appointment assigned to us in accordance with Art. 2 of D.P.R. No. 136, 1975, we have examined the balance sheet at June 30, 1985 and the profit and loss account for the year then ended, of Perugina S.p.A., which include the Directors' Report and those supplementary schedules required by Par. 4 of Art. 2424 of the Civil Code.
2. Our examination has been made in accordance with the auditing standards stated in the "Principi di Revisione" (from No. 1 to No. 17) approved by the "Consigli Nazionali dei Dottori Commercialisti e dei Ragionieri," performing those auditing procedures on the accounting records and on the valuation of the Company's assets that we considered necessary to fulfill our appointment. These procedures have involved our professional judgment on both the application of the accounting principles with which business transactions have been reflected in the accounting records and stated in the financial statements, and on the nature and extent of our audit tests of the accounting records and of all other documents and information in order to be in a position to issue, with due care and sufficient documentation, the requested opinion on the financial statements taken as a whole. In designing our tests we have considered the degree of reliance which could be placed on internal accounting controls and the subsequent

*Translated from the Italian.

valuation of the risk that the financial statements, taken as a whole, might be affected by errors, irregularities or illegal acts. The accounting principles to which we have referred in order to express our opinion on the financial statements of the Company are those issued by the "Consigli Nazionali dei Dottori Commercialisti e dei Ragionieri," and, for the ones not yet existing, those issued by the International Accounting Standards Committee (I.A.S.C.).

Our examination has also included the Directors' Report in its entirety. However, considering the extent of coverage of this report, our opinion is only relevant to the data and that information necessary for the clarity and the precision of the financial statements, described in this particular case in the parts concerning the notes to the financial statements.

The examination of the supplementary schedules required as an appendix to the financial statements by Art. 2424 of the Civil Code was carried out only as far as was necessary to enable an opinion to be expressed on the financial statements of the Company, and thus such an opinion is not applicable to the supplementary schedules.

The final statements at June 30, 1984 are included for comparatives and were examined by us in the past. The opinion concerning those statements was issued on October 9, 1984.

3a. As indicated in the notes included in the Directors' Report, the Company has material, commercial and financial transactions with its parent company and other Group companies.

As described in Note 9 included in the Directors' Report, the indirect investment in two wholly owned companies is shown in the financial statements of their parent company, Perugina Corporation of America, at a value which is approximately US $7.7 million greater than the value that would have been obtained had the equity method been applied. Therefore the holding of Perugina S.p.A. in Perugina Corporation of America is also overstated by about Lit. 11,203 million in comparison with the value of the net equity of that subsidiary. This amount represents the excess cost paid by Perugina Corporation of America to Buitoni S.p.A. at the moment of acquisition. The price for this purchase was established by an agreement between the companies of the same Group which took into consideration the values indicated by an independent appraisal.

3b. As described in Note 2, in the course of the 1984/85 financial year, the Company altered the method used to determine costs related to internal construction and the accounting treatment of research and development expenditure and of financial charges incurred for the purchases of new assets, this in order to conform to the controlling Group's policies. Consequently, the net profit for the year is lower than it would have been using the method of calculation and accounting principles adopted in previous years, by about Lit. 1,870 million.

3c. The time required for the preparation of consolidated financial statements has prevented the Company from preparing these in time for presentation to the Meeting of Shareholders; nevertheless, consolidated financial statements are being prepared at the time of this report and will be completed within the terms envisaged. According to the accounting principles of which in the preceding paragraph 2, we consider that, in case of companies which have significant controlling shareholdings, supplementation of the financial statements for the year with the consolidated statements for the Group is necessary for an adequate presentation of the financial position and of the profit and loss situation, as well as of changes in the financial position of the Company and of the Group.

Since in the light of a restrictive interpretation of the principle of clarity and precision of which in Art. 2423 of the Civil Code, which for the moment predominates, the presentation of consolidated financial statements for the Group to supplement those of the Group Parent Company is not required, we have not considered that the omission mentioned above is not in itself such as to preclude the issuance of an opinion in accordance with Art. 4 of D.P.R. No. 136 dated March 31, 1975.

On page 6 of the Directors' Report, the difference between the value shown for shareholdings in subsidiaries and other Group companies and the value which would have been obtained using the equity method is shown.

4. Taking into account whatever mentioned heretofor as an integral part of our opinion, in accordance with D.P.R. No. 136 dated March 31, 1975, we certify that the balance sheet and the profit and loss account of Perugina S.p.A. for the year ended June 30, 1985 which include the Directors' Report as indicated in paragraph 2, are in agreement with the accounting records and conform to the results of audit procedures performed and to the legal requirements for balance sheet and profit and loss account presentation and that the underlying transactions are recorded in the above records, on the basis of correct accounting principles.

ARTHUR YOUNG & COMPANY

David Dell'Ariccia Mauro Castelli
(Partners)

Rome, October 2, 1985

BALANCE SHEETS
As at June 30, 1985 and 1984

	1984/1985 (Lire)	*1983/1984 (Lire)*
ASSETS		
Property, plant and equipment		
Land and buildings	22,175,707,014	21,148,479,014
Plant and machinery	60,000,205,816	53,719,172,942
Equipment	6,350,771,963	4,778,384,963
Office furniture and equipment	127,804,020	81,667,620
Vehicles	4,476,000	4,476,000
Construction in progress	8,762,691,172	10,003,044,287
	97,421,655,985	89,735,224,826
Goodwill	6,792,265,333	7,791,966,000
Trademarks	270,935,520	406,406,340
Deferred charges	4,418,623,357	4,792,123,999
Inventories		
Raw materials	17,009,368,269	14,219,169,266
Work in process and finished goods	38,240,258,000	28,277,417,000
	55,249,626,269	42,496,586,266
Cash	53,800,461	17,917,105
Investments	13,415,693,065	13,136,533,600
Marketable securities	50,000,001,465	—
Receivables		
Trade	23,230,998,137	14,503,696,383
Parent company–notes account	6,993,698,636	9,127,668,946
Parent company–current account	6,915,493,270	69,812,690,505
Group companies–trade account	7,658,888,778	9,478,510,785
Others	6,375,544,291	12,412,822,678
	51,174,623,112	115,335,389,297
Prepaid expenses	1,835,217,277	1,637,395,384
Total assets	280,632,441,844	275,349,542,817
Memo accounts		
Directors' guarantee deposits	2,000,000	1,800,000
Employees' guarantees	1,187,944,178	1,292,561,252
Guarantee deposits	35,000,000	35,000,000
	1,224,944,178	1,329,361,252

(Continued on next page.)

BALANCE SHEETS *(cont.)*

	1984/1985 (Lire)	*1983/1984 (Lire)*
LIABILITIES		
Capital stock		
Ordinary shares	51,000,000,000	51,000,000,000
Savings shares	17,000,000,000	17,000,000,000
	68,000,000,000	68,000,000,000
Other equity accounts		
Legal reserve	10,044,031,704	9,487,750,799
Distributable reserve	4,692,680,053	4,663,342,855
Reserve ex lege 19/3/83 No. 72	5,432,291,000	5,432,291,000
Capital in excess of par value	6,438,169,755	6,438,169,755
Undistributed earnings	81,556,721	81,556,721
VAT special deduction	191,251,813	188,251,813
	26,879,981,046	26,291,362,943
Accumulated depreciation		
Buildings	2,072,742,307	1,491,732,949
Plant and machinery	23,198,148,566	16,068,703,154
Equipment	3,406,761,355	2,194,661,026
Office furniture and equipment	45,120,399	31,613,047
Vehicles	3,159,666	2,366,466
	28,725,932,293	19,789,076,642
Allowance for doubtful accounts	1,288,135,646	860,000,023
Income taxes payable	7,828,000,000	10,061,000,000
Accrued employees' leaving indemnities	25,247,240,799	23,062,405,761
Current portion of long-term debt from parent company	1,520,646,558	1,277,809,270
Current portion of outside long-term debt	22,000,000,000	—
Long-term debt from parent company	6,080,105,334	7,600,751,892
Long-term debt	—	22,000,000,000
Debenture bonds 15%	25,500,000,000	25,500,000,000
Long-term notes payable	1,829,017,934	1,644,284,542

VAT = value-added tax.

	1984/1985 (Lire)	1983/1984 (Lire)
Payables		
Banks	—	5,014,390,388
Trade	22,562,538,043	24,802,223,217
Group companies–trade account	1,615,504,583	9,394,428,663
Others	31,001,442,329	13,166,724,985
	55,179,484,955	52,377,767,253
Accrued liabilities	5,337,433,917	5,759,466,388
Net income for the year to date	5,216,463,362	11,125,618,103
Total liabilities	280,632,441,844	275,349,542,817
Memo accounts		
Directors for guarantee deposits	2,000,000	1,800,000
Banks for employees' guarantees	1,187,944,178	1,292,561,252
Third parties for guarantee deposits	35,000,000	35,000,000
	1,224,944,178	1,329,361,252

STATEMENTS OF PROFIT AND LOSS ACCOUNTS
Years Ended June 30, 1985 and 1984

	1984/1985 (Lire)	*1983/1984 (Lire)*
INCOME		
Revenues		
Sales of products	255,344,603,384	240,342,129,593
Sales of by-products and scrap	708,356,436	550,124,375
Sales of materials	554,563,808	814,062,165
Services	3,422,902,589	1,080,042,826
Total revenues net of discounts	260,030,426,217	242,786,358,959
Interest from trade receivables	1,597,972,764	1,331,916,340
Interest from other receivables	311,503	5,132,283
Interest from parent company–current account	7,093,046,766	6,683,415,856
Interest from marketable securities	464,000,000	—
Gain on sale of fixed assets	1,900,000	15,334,000
Gain on investments	279,159,465	—
Other income	2,145,073,082	1,298,725,630
Other income related to prior years	414,051,845	908,601,306
Exchange gain	1,334,373,940	503,967,263
Internal construction	9,952,745,259	14,395,343,032
Ending inventories of raw materials, work in process and finished goods	55,249,626,269	42,496,586,266
Total	338,562,687,110	310,425,380,935
EXPENSES		
Beginning inventories of raw materials, work in process and finished goods	42,496,586,266	43,222,522,648
Purchases of raw materials, work in process and finished goods	125,926,216,974	99,499,872,387

	1984/1985 (Lire)	*1983/1984 (Lire)*
Labor and related social contributions	61,468,734,658	55,374,461,171
Manufacturing overhead, selling and general expenses	65,922,780,167	62,648,654,115
Income taxes	4,882,000,000	10,061,000,000
Interest on long-term debt from parent company	1,577,716,104	1,756,205,979
Interest on long-term debt (outside)	4,567,400,375	1,870,717,550
Interest on convertible bonds	3,825,000,000	3,825,000,000
Interest on other payables	702,347,400	915,784,266
Discounts and other financial charges	1,718,396,410	1,575,555,209
Exchange loss	158,315,361	328,218,210
Other costs and expenses	245,440,028	2,333,522
Depreciation and amortization		
Buildings	581,009,358	534,060,806
Plant and machinery	7,198,738,412	6,148,843,790
Equipment	1,212,100,329	862,596,866
Office furniture and equipment	13,507,352	9,776,474
Vehicles	6,223,200	793,200
Deferred charges	2,593,013,352	1,601,814,655
Goodwill	999,700,667	999,700,667
Trademarks	135,470,820	135,476,940
	12,739,763,490	10,293,063,398
Provision for employees' leaving indemnity	5,850,113,358	4,633,580,773
Provision for doubtful receivables	700,014,759	683,368,500
Other expenses related to prior years	536,220,648	429,920,304
Loss on investments	—	1,961,216,400
Loss on sale of fixed assets	29,177,750	218,288,400
Net income	5,216,463,362	11,125,618,103
Total	338,562,687,110	310,425,380,935

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Years Ended June 30, 1985 and 1984

	Total Shareholders' Equity (Lit.)	*Capital Stock (Lit.)*	*Legal Reserve (Lit.)*	*Distributable Reserve (Lit.)*
Balance as at June 30, 1983	100,263,117,201	68,000,000,000	8,933,000,000	4,663,077,666
Utilization of net income for the year 1982/83 as approved by the Shareholders' Meeting of November 30, 1983	(6,120,000,000)	—	554,750,799	265,189
VAT special deduction	148,245,742	—	—	—
Net income for the year 1982/83	11,125,618,103	—	—	—
Balance as at June 30, 1984	105,416,981,046	68,000,000,000	9,487,750,799	4,663,342,855
Utilization of net income for the year 1983/84 as approved by the Shareholders' Meeting of November 8, 1984	(10,540,000,000)	—	556,280,905	29,337,198
VAT special deduction	3,000,000	—	—	—
Net income for the year 1984/85	5,216,463,362	—	—	—
Balance as at June 30, 1985	100,096,444,408	68,000,000,000	10,044,031,704	4,692,680,053

Capital in Excess of Par Value (Lit.)	*Undistributed Earnings (Lit.)*	*VAT Special Deductions (Lit.)*	*Reserve ex Lege 19/3/83 n. 72 (Lit.)*	*Interim Dividend (Lit.)*	*Net Income (Lit.)*
6,438,169,755	81,556,721	40,006,071	5,432,291,000	(4,420,000,000)	11,095,015,988
—	—	—	—	4,420,000,000	(11,095,015,988)
—	—	148,245,742	—	—	—
—	—	—	—	—	11,125,618,103
6,438,169,755	81,556,721	188,251,813	5,432,291,000	—	11,125,618,103
—	—	—	—	—	(11,125,618,103)
—	—	3,000,000	—	—	—
—	—	—	—	—	5,216,463,362
6,438,169,755	81,556,721	191,251,813	5,432,291,000	—	5,216,463,362

RECLASSIFIED BALANCE SHEETS
As at June 30, 1985 and 1984

	1984/1985 (Lire)	*1983/1984 (Lire)*
ASSETS		
Current assets		
Cash	53,800,461	17,917,105
Receivables		
Trade (less allowance for doubtful accounts of Lit. 1,288,135,646 and Lit. 860,000,023 as at June 30, 1985 and 1984, respectively)	21,942,862,491	13,643,696,360
Parent company–notes account	6,993,698,636	9,127,668,946
Parent company–current account	6,915,493,270	69,812,690,505
Group companies–trade account	7,658,888,778	9,478,510,785
Others	6,375,544,291	12,412,822,678
	49,886,487,466	114,475,389,274
Marketable securities	50,000,001,465	—
Inventories		
Raw materials	17,009,368,269	14,219,169,266
Work in process and finished goods	38,240,258,000	28,277,417,000
	55,249,626,269	42,496,586,266
Prepaid expenses	1,835,217,277	1,637,395,384
Total current assets	157,025,132,938	158,627,288,029
Property, plant and equipment	97,421,655,985	89,735,224,826
Less accumulated depreciation net property, plant and equipment	(28,725,932,293)	(19,789,076,642)
	68,695,723,692	69,946,148,184
Goodwill	6,792,265,333	7,791,966,000
Investments	13,415,693,065	13,136,533,600
Trademarks	270,935,520	406,406,340

	1984/1985 (Lire)	1983/1984 (Lire)
Deferred charges	4,418,623,357	4,792,123,999
Total assets	250,618,373,905	254,700,466,152
Memo accounts	1,224,944,178	1,329,361,252
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Banks	—	5,014,390,388
Payables		
Trade	22,562,538,043	24,802,223,217
Group companies	1,615,504,583	9,394,428,663
Others	20,209,420,329	13,166,724,985
	44,387,462,955	47,363,376,865
Income taxes payable	7,828,000,000	10,061,000,000
Accrued liabilities	5,337,433,917	5,759,466,388
Current portion of long-term notes payable	505,435,163	224,905,028
Current portion of outside long-term debt	22,000,000,000	—
Current portion of long-term debt from parent company	1,520,646,558	1,277,809,270
Debenture bonds (current portion)	103,800,000	—
Total current liabilities	81,682,778,593	69,700,947,939
Long-term debt	—	22,000,000,000
Long-term debt from parent company	6,080,105,334	7,600,751,892
Long-term notes payable	1,323,582,771	1,419,379,514
Long-term debt	10,792,022,000	—
Debenture bonds	25,396,200,000	25,500,000,000
Accrued employees' leaving indemnities	25,247,240,799	23,062,405,761
Total liabilities	150,521,929,497	149,283,485,106

(Continued on next page.)

RECLASSIFIED BALANCE SHEETS *(cont.)*

	1984/1985 (Lire)	*1983/1984 (Lire)*
Shareholders' equity		
Capital stock	68,000,000,000	68,000,000,000
Legal reserve	10,044,031,704	9,487,750,799
Distributable reserve	4,692,680,053	4,663,342,855
Reserve ex lege 19.3.83 No. 72	5,432,291,000	5,432,291,000
Capital in excess of par value	6,438,169,755	6,438,169,755
Undistributed earnings	81,556,721	81,556,721
VAT special deduction	191,251,813	188,251,813
Net income for the year to date	5,216,463,362	11,125,618,103
Total shareholders' equity	100,096,444,408	105,416,981,046
Total liabilities and shareholders' equity	250,618,373,905	254,700,466,152
Memo accounts	1,224,944,178	1,329,361,252

RECLASSIFIED PROFIT AND LOSS ACCOUNTS
Years ended June 30, 1985 and 1984

	1984/1985 (Lire)	*1983/1984 (Lire)*
Net sales	260,030,426,217	242,786,358,959
Adjustments to carrying value of investments	279,159,465	(1,961,216,400)
Costs and expenses		
Cost of sales (excluding depreciation)	171,993,610,578	151,717,963,296
General and administrative expenses	21,577,279,100	19,933,000,000
Selling expenses	42,414,184,976	38,251,000,000
Research and development	1,177,000,000	320,000,000
Depreciation and amortization	12,739,763,490	10,293,063,398
	249,901,838,144	220,515,026,694
Operating income	10,407,747,538	20,310,115,865
Other income (expenses)		
Interest income	9,155,331,033	8,020,464,479
Interest expense	(12,390,860,289)	(8,891,830,004)
Other income	3,895,398,867	2,726,628,199
Other expenses	(969,153,787)	(978,760,436)
	(309,284,176)	876,502,238
Income before taxes	10,098,463,362	21,186,618,103
Income taxes	4,882,000,000	10,061,000,000
Net income	5,216,463,362	11,125,618,103

STATEMENTS OF CHANGES IN FINANCIAL POSITION
Years ended June 30, 1985 and 1984

	1985/1984 (Lire)	*1984/1983 (Lire)*
Sources		
Net income for the year	5,216,463,362	11,125,618,103
Adjustments for items not affecting working capital		
Results of investments	(279,159,465)	1,961,216,400
Depreciation and amortization	12,739,763,490	10,293,063,398
Provision for employees' leaving indemnity	5,850,113,358	4,633,580,773
Working capital provided by operations	23,527,180,745	28,013,478,674
Net book value of property, plant and equipment sold	229,724,326	249,080,400
Increase of long-term loans	—	22,000,000,000
Increase of long-term notes payable	409,638,420	1,644,284,542
Increase of long-term debt	10,792,022,000	—
Increase of other reserves	3,000,000	148,245,742
	34,961,565,491	52,055,089,358
Applications		
Purchase of property, plant and equipment	10,048,465,485	14,395,343,032
Increase of deferred charges	161,925,710	2,626,506,580
Payment of employees' leaving indemnities	3,665,278,320	439,264,364
Transfer of current portion of long-term notes payable to current liabilities	505,435,163	224,905,028
Transfer of current portion of long-term debt from parent company to current liabilities	1,520,646,558	1,277,809,270
Transfer of current portion of long-term debt to current liabilities	22,000,000,000	—
Transfer of current portion of debenture loan to current liabilities	103,800,000	—
Dividends paid	10,540,000,000	6,120,000,000
	48,545,551,236	25,083,828,274

	1985/1984 (Lire)	*1984/1983 (Lire)*
Increase (decrease) in net working capital	(13,583,985,745)	26,971,261,084
Increase (decrease) in components of working capital		
Current assets		
Cash	35,883,356	1,081,626
Receivables	(64,588,901,808)	47,104,322,079
Marketable securities	50,000,001,465	—
Inventories	12,753,040,003	(725,936,382)
Prepaid expenses	197,821,893	507,301,699
	(1,602,155,091)	46,886,769,022
Current liabilities		
Banks	(5,014,390,388)	5,014,390,388
Payables	(2,975,913,910)	11,199,357,801
Income taxes payable	(2,233,000,000)	2,327,211,000
Accrued liabilities	(422,032,471)	1,086,733,801
Current portion of long-term debt	22,627,167,423	287,814,948
	11,981,830,654	19,915,507,938
Increase (decrease) in net working capital	(13,583,985,745)	26,971,261,084

EXPLANATORY NOTES TO THE FINANCIAL STATEMENTS
As at June 30, 1985

1. Nature of the Business

The Company's business, both in Italy and abroad and also on behalf of third parties, consists of the following:

- the manufacture and sale of any confectionery or food product.

It may perform the following activities whenever these are necessary, useful or desirable for the attainment of its object:

- the acquisition, use and sale of patents;
- the acquisition, construction, sale and lease of movable and real estate;
- the formation of new companies as well as the acquisition and sale of investments in companies and enterprises;
- any other industrial, commercial, financial, credit, movable and real estate transactions, including guarantees in favor of third parties.

2. Major Accounting Policies

Property, Plant and Equipment

Property, plant and equipment transferred by Buitoni S.p.A. (once IBP Industrie Buitoni Perugina S.p.A.) during 1981 (shown at the appraisal value) and that originally owned by Ultra S.p.A. or purchased after the transfer (shown at cost), were revalued during the year ended June 30, 1983 by approximately Lit. 6,303 million, as permitted by Law No. 72 of March 19, 1983 (Visentini bis).

The value of the revalued assets is not higher than that determined on the basis of their future possibility of utilization in the Company's activity.

The Company capitalizes costs related to internal constructions. For the year 1984/85 such capitalization amounts to approximately Lit. 414 million. For the year 1984/85 the Company, in order to conform to the Group's policies, changed the method of calculation; this resulted in a lower capitalization of approximately Lit. 1,290 million.

Financial charges incurred for the purchase of new fixed assets until they are ready for use were being capitalized until June 30, 1984. For the year 1984/85 the Company, in order to conform to the Group's policies and considering the present fiscal legislation, has not capitalized financial charges. The effect of the change in accounting principle resulted in a non-capitalization of approximately Lit. 1,170 million.

Renewals and betterments that extend the useful life of property, plant and equipment are capitalized.

Depreciation

Depreciation is provided using the straight line method, at percentages allowed for tax purposes. Such rates, which reflect the estimated useful lives of the related assets, are as follows:

Buildings	3%
Plant and machinery	12.5%–14%
Equipment	20%–25%
Office furniture and equipment	12%
Vehicles	20%

Inventories

Raw materials, work in progress and finished goods are stated at the lower of cost (FIFO) or market at year-end.

Investments

The investment in a wholly owned U.S.A. company is carried at the purchase price, adjusted on the basis of the results of the year.

Deferred Charges

Deferred charges relate mainly to the following:

a. Research and development costs incurred until June 30, 1984, deferred to the extent of 75% and amortized using the straight line method over the subsequent three years. For the year 1984/85 the Company, in order to conform to the Group's policies, has not capitalized such costs, with a consequent non-capitalization for approximately Lit. 970 million.

b. Costs incurred in connection with various capital stock increases which are amortized using the straight line method over five years.

c. Interest costs, net of the contribution provided by Law No. 1329/65, on outstanding instalments for purchases of fixed assets according to the Sabatini Law, amortized at constant rates over the period of deferral. The amount capitalized in the year is Lit. 51 million.

d. Advertising expenses incurred during 1983/84 with respect to the development of commercial activities in the U.S.A., amortized at constant rates over three years.

e. Restructuring and start-up costs related to the new office premises deferred to the extent of 80% and amortized, at constant rates, over the following four years.

f. Costs incurred during 1983/84 for the reorganization of EDP and office automation, deferred to the extent of 80% and amortized at constant rates over the following four years.

Trademarks

Trademarks, originally shown at cost, are amortized using the straight line method over five years.

Goodwill

The cost of goodwill, related to the spin-off to the Company by Buitoni S.p.A., of the assets and liabilities of its confectionery division, is amortized using the straight line method over ten years.

Marketable Securities

Marketable securities, consisting of State Bonds, are carried at cost; interest accrued at year-end is included in accrued income.

Receivables

Receivables are carried at their face value adjusted by a specific allowance for doubtful accounts sufficient to cover all expected losses.

Income Taxes Payable

The income taxes payable correspond to the estimated income tax liability.

Accrued Employees' Leaving Indemnity

This fund reflects the actual liability of the Company towards its personnel on the basis of their legal position as at June 30, 1985, taking into account the provisions for Law No. 297/82.

Foreign Currency Transactions

Transactions in foreign currencies are translated at the rates of exchange prevailing at the time when the transaction took place. Payables and receivables expressed in foreign currencies are translated at the rates of exchange prevailing on June 30, 1985. The resulting gain or loss is taken in the Profit and Loss Account.

Reclassified Balance Sheet

In the reclassified Balance Sheet assets and liabilities are classified as current and non-current based on the criterion of an annual operating cycle.

3. Receivables From Parent Company–Notes Account

Receivables from the parent company–notes account consist of notes and drafts drawn on customers transferred for cashing subject to collection, to the parent company.

4. Receivables From Parent Company–Current Account

Most receipts and payments are made by the parent company using a specific current account bearing an interest rate of 20% per annum for the second half of 1984 and 16.5% per annum for the first half of 1985.

5. Receivables From and Payables to Group Companies–Trade Account

Receivables from and payables to Group companies–trade account, as at June 30, 1985 include the following (in millions of lire):

Receivables from parent company	3,307
Receivables from subsidiary	4,240
Receivables from other Group companies	112
Receivables from Group companies	7,659
Payables to parent company	163
Payables to other Group companies	1,452
Payables to Group companies	1,615

6. Balances in Foreign Currency

As of June 30, 1985 the Company shows a receivable from its subsidiary Perugina Chocolate & Confections Inc., of approximately U.S. $2,174,000. The rate of exchange used is Lit. 1949.95 to 1 U.S. $, the official Italian rate at June 30, 1985 (UIC rate).

7. Other Receivables

Other receivables as at June 30, 1985 include the following (in millions of lire):

Advances to employees for salaries and wages	3,264
Advances to suppliers	1,398
Sugar rebate	494
Others	1,219
	6,375

8. Inventories

Work in process and finished goods included in inventories are as follows (in millions of lire):

Work in process	6,182
Finished goods	32,058
	38,240

9. Investments

This balance relates to a wholly owned U.S.A. subsidiary, Perugina Corporation of America, purchased during the year ended June 30, 1983 at a price of U.S. $10,000,000 equal to Lit. 15,098 million. This amount has been reduced, during 1983/84, by Lit. 1,961 million, and has been increased, during 1984/85, by Lit. 279 million, to account for the results reported by the company and its subsidiaries Perugina Chocolate & Confections Inc. and Perugina Shoppes Inc. The rate of exchange used is that of the purchase price equal to Lit. 1509.8 to 1 U.S. $. Prudently, and considering the present fiscal legislation for which such revaluations are part of the taxable income, no adjustment has been made to account for the increase in the rate of exchange of the U.S. $ with respect to the Italian lira, which would have led to a revaluation of this investment of Lit. 3,900 million at the rate of exchange prevailing on June 30, 1985. In the financial statements of Perugina Corporation of America as at June 30, 1985, the value of the investment in its subsidiaries is higher than their shareholders' equities by approximately $7.7 million.

In detail (U.S. $ thousands):

	Perugina Chocolate & Confections Inc.	*Perugina Shoppes Inc.*	*Total*
Book value	7,903	983	8,886
Shareholders' equity	884	251	1,135
Overstatement	7,019	732	7,751

Consequently, the investment of Perugina S.p.A. in Perugina Corporation of America Inc. as at June 30, 1985, overstated as follows:

	U.S. $ (thousands)	*Rate of exchange*	*Italian lire (millions)*
Book value	8,886	1,509.8	13,416
Shareholders' equity	1,135	1,949.9	2,213
Overstatement	7,751		11,203

The above mentioned overstatements are equivalent to the excess value paid by Perugina Corporation of America to the holding company Buitoni S.p.A. at the purchase date.

The price paid was based upon an independent appraisal by Lehman Brothers Kuhn Loeb, one of the leading merchant banks in the United States of America.

The Directors, on the basis of their prudent judgement, consider that the book value of these investments is not excessive.

10. Capital Stock

The capital stock as at June 30, 1985 consists of 51,000,000 ordinary and 17,000,000 savings shares with a par value of Lit. 1,000 each. Buitoni S.p.A. owns approximately 83.5% of the ordinary shares.

11. Reserves

The following is the classification of reserves and other equity accounts as at June 30, 1985 as required by art. 2 of Law No. 649 of November 25, 1983.

1. Reserves and other equity accounts created, from fiscal year 1983/84 on, utilizing profits subjected to IRPEG (income tax on companies):	
• Legal reserve	556,280,905
• Distributable reserve	29,337,198
2. Reserves and other equity accounts created, from fiscal year 1983/84 on, utilizing profits not subjected to IRPEG:	0
3. Reserves or other equity accounts in existence at the end of the last fiscal year ended before December 1, 1983 or created utilizing profits of that year:	
• Legal reserve (net of the portion of capital in excess of par value reclassified in the amount of Lit. 8,461,830,425)	1,025,920,554
• Distributable reserve	4,663,342,855
• Undistributed earnings	81,556,721
4. Reserves or other equity accounts which, if distributed, should be added to the taxable income of the Company regardless of the period in which they were created:	
• VAT special deduction	191,251,813
• Reserve ex lege No. 72/83	5,432,291,000
5. Reserves or other equity accounts which, if distributed, should not be added to the taxable income of the shareholders independently of the period in which they were created:	
• Capital in excess of par value (of which the amount of Lit. 8,461,830,245 reclassified from legal reserve)	14,900,000,000

The legal reserve is not distributable and, if used for any reason, must be reintegrated. Capital in excess of par value is not distributable until the legal reserve amounts to one-fifth of capital stock.

12. Monetary Revaluation

During the year ended June 30, 1983 the Company revalued its property, plant and equipment as permitted by Law No. 72 of March 19, 1983 (Visentini bis), using the direct method.

As described by art. 10 of the above mentioned Law, indicated below is the residual amount of such revaluations relative to the assets in the balance sheet at June 30, 1985 (in millions of lire):

	Revaluation amount		
	Original cost	Disposals	Residual
Property, plant and equipment	6,303	(51)	6,252
Accumulated depreciation	(871)	7	(864)
	5,432	(44)	5,388

No provision for income taxes has been made with respect to this monetary revaluation reserve as it is not taxable unless distributed to the stockholders.

13. Income Taxes

The Company has settled its income taxes with the fiscal authorities through 1981 inclusive, on the basis of the automatic amnesty procedure provided by art. 19 of Decree No. 429 of July 19, 1982, converted into Law No. 516 of August 7, 1982.

14. Convertible Bonds

At June 30, 1985, 255,000 convertible bonds with a nominal value of Lit. 100,000 each, bearing interest at a semi-annual rate of 7.5%, were outstanding.

As presented by art. 7 of the Debenture Deed, the Board of Directors of the Company resolved, on March 13, 1985, to reimburse totally and in advance the 255,000 bonds. The reimbursement date has been fixed at July 1, 1985, with the option for the bondholders to convert, during June 1985, their bonds into savings shares of Perugina S.p.A. receiving for each three bonds owned 200 savings shares with a par value of Lit. 1,000 each.

Savings shares issued for conversion have as issue date, July 1, 1985. As of July 14, 1985 the bonds converted were 253,962.

15. Long-Term Debts

Long-term debts as at June 30, 1985 are as follows (in millions of lire):

	Outstanding debt
• Loan granted by Buitoni S.p.A., 11.5% interest per annum, repayable in semi-annual instalments through July 1, 1987	623

• Loan granted by Buitoni S.p.A., 19.5% interest per annum, repayable in semi-annual instalments through April 1, 1989	6,978
• Total long-term debts due to parent company	7,601
• Less current portion	1,521
• Non-current portion	6,080
• Loan granted by Citibank N.A. 17.9% interest per annum, payable on July 30, 1985 in the amount of	22,000
• Total long-term debts with third parties	22,000
• Less current portion	22,000
• Non-current portion	—
• Total long-term debts	6,080

16. Other Payables

Other payables as at June 30, 1985, include the following (in millions of lire):

• Social security institutions	15,705
• Salaries and wages and related deductions	8,200
• Customs	1,190
• Interest on debenture bonds	1,965
• Advance payments from customers	3,116
• Others	825
	31,001

17. Accrued Liabilities

Accrued liabilities as at June 30, 1985, include the following (in millions of lire):

• Deferred personnel remuneration and related contributions	2,879
• Financial charges	991
• Reserve for returns	803
• Others	664
	5,337

18. Transactions With Parent Company, Subsidiaries and Other Group Companies

During the financial year the Company had significant commercial transactions with its parent company, its subsidiaries and other Group companies at conditions which reflect normal market conditions, for the following amounts (in millions of lire):

Transactions with parent company:	
• Sales	19,969
• Purchases of raw material	43,747
• Purchases of services	12,007
Transactions with subsidiaries:	
• Sales	13,231
Transactions with Group companies:	
• Purchases of materials	12,530

APPENDIX D

Checklist for Comparison of Generally Accepted Auditing Standards (GAAS) in the United States to Auditing Standards in Italy

General Questions	Answer	Comments
1. Is a primary purpose of an audit—		1. The primary purpose is to attest to information used by third parties.
a. To attest to information used by investors, creditors, and so forth?	Yes	
b. To satisfy statutory requirements (for example, the Companies Act)?	Yes	
c. For tax purposes?	Yes	
2. A. The United States has ten generally accepted auditing standards, including general standards, standards of fieldwork, and standards of reporting. Those standards and their interpretations constitute	Yes	

Notes:

Checklist should be completed from the perspective of performing a local audit, *not* a referral audit.
AU numbers refer to sections in the AICPA's *Codification of Statements on Auditing Standards* unless otherwise noted.
PR = Principi revisione (auditing standards).

General Questions	Answer	Comments
U.S. generally accepted auditing standards, which have been published in *Codification of Statements on Auditing Standards*. Do generally accepted auditing standards exist in Italy?		
B. If so, are they published?	Yes	
C. If auditing standards exist in Italy, are they similar to U.S. standards?	Yes	
D. If not, what are they?		2D. Italian auditing standards are similar to U.S. standards except for the following: • The consistency paragraph is not used, since consistency is implied; disclosure of inconsistency is part of the generally accepted accounting principles. • Standards of reporting issued today do not cover non full scope audits.
3. Who is responsible for promulgating auditing standards (for example, the profession? a governmental body)?		3. The profession and Consob (the equivalent of the SEC) can recommend the adoption of Auditing Standards.

U.S. Generally Accepted Auditing Standards	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
4. Do auditors confirm receivables? (AU sec. 331)	Yes. PR no. 7	✓			
5. Do auditors observe inventory counts? (AU sec. 331)	Yes. PR no. 6	✓			
6. Do auditors receive written representations from management? (AU sec. 333)	Yes. PR no. 4	✓			
7. Do auditors receive written representations from management's legal counsel? (AU sec. 337)	Yes. PR no. 4	✓			
8. A. Do auditors prepare and maintain working papers? (AU sec. 339)	Yes. PR no. 4	✓			
B. If so, do they include a written audit program outlining procedures to be performed? (AU sec. 339)	Yes. PR no. 4	✓			
9. Do auditors study existing internal controls as a basis for reliance thereon in determining the nature, extent, and timing of audit tests to be performed? (AU sec. 320)	Yes. PR no. 3	✓			
10. A. Do auditors communicate material weaknesses in internal accounting control to senior management or the client's board of directors? (AU sec. 323)	Yes. PR no. 2	✓			

U.S. Generally Accepted Auditing Standards	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
B. If so, is the communication documented? (AU sec. 323)	Yes. PR no. 2	✓			
11. In obtaining evidential matter, does the auditor apply either statistical or nonstatistical procedures? (AU sec. 350)	Yes. PR no. 3	✓			
12. Is the auditor responsible for planning his examination to search for errors or irregularities that would have a material effect on the financial statements? (AU sec. 327)	Yes. PR no. 2	✓			
13. A. Does the auditor perform procedures to identify related party transactions and their effect on the financial statements? (AU sec. 334)	Yes. Civil Code	✓			13A,B. The Civil Code does not specify procedures to be performed, but does require disclosure of related parties. It is common practice to follow U.S. standards on procedures concerning related parties.
B. If so, list the procedures.					
14. Does the auditor consider the adequacy of cut-off procedures to insure that movements into and out of inventories are properly identified in the accounting records? (AU sec. 313)	Yes. PR no. 6	✓			
15. A. Are specific auditing procedures applied to transactions occurring after the balance sheet date? (AU sec. 560)	No	✓			

B. Are other auditing procedures applied to ascertain the occurrence of subsequent events that require adjustment to or disclosure in the financial statements? (AU sec. 560)	No	✓	
16. The concept of "joint auditors" in certain countries (for example, U.K., Canada, and Australia) is that two auditors or audit firms jointly audit the financial statements of a company and issue a single report signed by the two firms. This practice is not generally followed in the U.S. Does the concept of "joint auditors" exist in Italy?	No		✓
17. When a principal auditor is reporting on financial statements that include one or more subsidiaries, divisions, branches, or investees: (AU sec. 543)			
A. Must the principal auditor assume responsibility for the work of the other auditor as it relates to the principal auditor's opinion?	No		✓
B. May the principal auditor decide not to assume that responsibility by making reference to the other auditor and indicating the division of responsibility?	Yes. PR no. 2	✓	

U.S. Generally Accepted Auditing Standards	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
18. A. Is there a standard form of auditor's report? (AU sec. 509)	Yes. Assirevi	✓			18A. There are alternative forms for consolidated financial statements. See appendix C for an example.
B. List the circumstances that require a departure from the standard report and indicate the type of report required. (AU sec. 509)				✓	18B. The majority of Italian companies get legal opinions because they are governed by legal rules. A legal opinion is a clean opinion with explanations; a qualified legal opinion is not permitted. For those companies not governed by legal requirements, auditing standard no. 18 applies and qualifications are permitted.
19. A. Does the auditor's report express an opinion on the consistency of application of accounting principles? (AU sec. 420)	No			✓	
B. If not, does it imply that either consistency exists or the financial statements disclose the inconsistency?	Yes. Assirevi	✓			
20. A. Is the auditor's report dated as of the last day of fieldwork? (AU sec. 530)	Yes. PR no. 18	✓			
B. If not, what date is used?					

21. To express an opinion, must the auditor be independent? For the purpose of this checklist, independence is defined as being free of financial interest in the client. (Code of Professional Ethics, Rule 101)	Yes. Italian law 136	✓	
22. Please describe any standards for Italy for which there are no corresponding U.S. standards.			22. Auditing procedures required in Italy but not in the United States follow: • Payables must be confirmed. • Cash must be counted.

APPENDIX E

Checklist for Comparison of Generally Accepted Accounting Principles (GAAP) in the United States to Accounting Principles in Italy

General Information	Answers	Comments
1. Are there generally accepted accounting principles in Italy? If so, are they codified?	Yes. They are codified (referred to).	
2. Who is responsible for promulgating accounting principles (for example, the profession, a governmental body, etc.)?	Profession	

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
3. Are assets and liabilities recorded on the historical cost basis?	Yes. PC no. 4	✓			
4. Are interest costs, incurred while activities that are necessary to get	Yes. PC no. 4	✓			

an asset ready for its intended use are in progress, capitalized as part of the historical cost of an asset? (I67)				
5. A. Is a general revaluation (either upward or downward) of assets permitted? (D40)	Yes. Italian law	✓		5A. Only by law.
B. If so, define the basis.				5B. Adoption of revaluation mark-up fixed by law.
6. Are nonmonetary transactions that culminate an earnings process accounted for on the basis of the fair market value of the assets involved when that value is determinable within reasonable limits? (N35)	Yes. PC no. 4		✓	6. Infrequent
7. Is revenue recognized when it is earned and its realization is reasonably assured (rather than when money is received)? (Statement of Financial Accounting Concepts No. 5)	Yes. PC no. 2	✓		
8. Are costs recorded when incurred rather than when money is paid? (Statement of Financial Accounting Concepts No. 5)	Yes. PC no. 2	✓		
9. A. Are consolidated financial statements required when one company has control over another company? (C51)	Yes. PC no. 8	✓		9A. Also IAS no. 3

Notes:

Parenthetic references are to sections in the *FASB Current Text*, unless otherwise noted.
PC = Principi contabili (accounting principles).

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
B. Is control usually indicated by ownership of over fifty percent of the outstanding voting shares? If not, how is control indicated?	Yes. PC no. 8	✓			9B. The concept of dominant influence to indicate control is also accepted.
10. A. Are there instances when an entity would not be consolidated even though control is present? (C51)	Yes. PC no. 8	✓			
B. If so, list them.					10B. Temporary investments and interest in foreign subsidiaries located in countries where the investment cannot be legally transferred.
11. If consolidation is not otherwise appropriate, is the equity method used for unconsolidated subsidiaries, corporate joint ventures, and other investees, if the investments give the investor the ability to exercise significant influence over the investees' operating and financial policies? (I82)	Yes. PC no. 8		✓		11. Cost is generally used for tax reasons.
12. Are there two methods of accounting for business combinations—the pooling-of-interests method and the purchase method? (B50)	Yes. IAS no. 22			✓	12. Only the purchase method is practiced or permitted in Italy, except in mergers, which are treated like poolings.

13. Is the method used to account for a business combination disclosed? (B50)	Yes. IAS no. 22			✓	
14. A. Do criteria exist for treatment of business combinations as poolings of interests? (B50)	Yes. IAS no. 22			✓	
B. If so, list the criteria.					14B. See IAS no. 22.
15. A. Is goodwill arising from a business combination accounted for as an asset? (I60)	Yes. PC. no. 8			✓	15. Included in investment.
B. If so, is it amortized as a charge to income over the period estimated to be benefited?	Yes. PC no. 8			✓	
16. Are the following disclosures made for related party transactions: (R36)					
a. The nature of the relationship?	Yes. IAS no. 24	✓			
b. A description of the transactions for the periods presented?	Yes. IAS no. 24	✓			
c. The amounts of the transactions for the periods presented?	Yes. IAS no. 24		✓		
d. The amounts due to or from related parties at the balance sheet date?	Yes. IAS no. 24	✓			
17. Is an estimated loss from a loss contingency accrued only if it is probable that an asset has been impaired or a liability incurred and the amount of loss can be reasonably estimated? (C59)	Yes. PC no. 7	✓			
18. If a loss contingency is not accrued because both conditions for accrual listed in question 17 are not met,	Yes. PC no. 7	✓			

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
is disclosure of the contingency required when there is at least a reasonable possibility that a loss may have been incurred? (C59)					
19. Are guarantees of the indebtedness of others or other loss contingencies disclosed in financial statements even though the possibility of loss may be remote? [In the U.S., guarantees are usually disclosed as loss contingencies even if the possibility of loss is remote.] (C59)	Yes. PC no. 7	✓			
20. Are the following items disclosed in an enterprise's financial statements for each industry segment: (S20)					
a. Sales to outsiders and intersegment sales?	Yes. IAS no. 14	✓			
b. Operating profit or loss?	Yes. IAS no. 14	✓			
c. Identifiable assets and related depreciation, depletion, and amortization expenses?	Yes. IAS no. 14	✓			
d. Capital expenditures?	Yes. IAS no. 14	✓			
e. Equity in net income and net assets of unconsolidated subsidiaries and other investees?	Yes. IAS no. 14	✓			

f. Effect of a change in accounting principle? (S20)	Yes. IAS no. 14	✓		
21. A. Are there any requirements to disclose the effects of inflation? (C27)	Yes. IAS no. 15		✓	
B. If so, list the disclosures required.				21B. See IAS no. 15 for disclosure requirements.
22. Are assets segregated into current and noncurrent classifications with a total for current assets presented? (B05)	Yes. PC no. 2	✓		
23. A. Are noncurrent assets those not expected to be realized within one year or the current operating cycle? (B05)	Yes. PC no. 2	✓		
B. If not, how are noncurrent assets defined?				
24. A. Is an allowance established for uncollectible receivables? (C59)	Yes. PC no. 6	✓		
B. If so, what is the basis (for example, percentage of sales, aging of receivables, and so forth) for calculating the allowance?				24B. The three methods used are specific identification, aging, and percentage of sales. Specific identification, either alone or combined with aging, is the predominant practice. Percentage of sales is the minority practice.
25. Are receivables and payables, not arising in the normal course of business or subject to normal trade terms, recorded at an amount which takes imputed interest into account? (I69)	Yes. PC no. 6	✓		

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
26. A. Is inventory stated at the lower of cost or market (or net realizable value)? (I78)	Yes. PC no. 3	✓			
B. If not, how is inventory stated?					
C. Is the basis disclosed?	Yes. PC no. 3	✓			
27. Does cost for inventory purposes include: (178)					
a. Materials?	Yes. PC no. 3	✓			
b. Direct labor?	Yes. PC no. 3	✓			
c. Factory overhead?	Yes. PC no. 3	✓			
d. If the añswer to *c.* is yes, is an allocable share of all factory overhead included?	Yes. PC no. 3	✓			
28. A. Are the following cost methods permitted for reporting purposes: (178)					28A,B. LIFO is usually adopted for tax purposes, but any other method resulting in an amount not lower than LIFO may be used.
a. First-in, first-out (FIFO)?	Yes. PC no. 3	✓			
b. Last-in, first-out (LIFO)?	Yes. PC no. 3	✓			
c. Average cost?	Yes. PC no. 3	✓			
B. Are the same methods permitted for tax purposes?	See Comments.				
29. Is the inventory costing method used disclosed? (178)	Yes. PC no. 3	✓			
30. A. Are fixed assets depreciated over their estimated useful lives by systematic charges to income? (D40)	Yes. PC no. 4	✓			

B. If so, is an accumulated depreciation account used?	Yes. PC no. 4	✓	
31. Are disclosures made of: (D40)			
a. Depreciation expense for the period?	Yes. PC no. 4	✓	
b. Balances of major classes of depreciable assets?	Yes. PC no. 4	✓	
c. The methods used to compute depreciation for the major asset classes?	Yes. PC no. 4	✓	
d. Accumulated depreciation, either by major class of assets or in total?	Yes. PC no. 4	✓	
32. A. Do criteria exist for classifying leases as operating leases? (L10)	Yes. IAS no.17	✓	32A,B. For tax purposes, only operating leases are permitted. See IAS no. 17 for disclosure requirements.
B. If so, list the criteria and disclosure requirements.			
33. A. Do criteria exist for classifying leases as other than operating leases for the lessor and lessee? (L10)	Yes. IAS no. 17		33A,B. See question 32, comments.
B. If so, list the criteria, type of lease, and disclosure requirements.			
34. Are liabilities segregated into current and noncurrent classifications with a total for current liabilities presented? (B05)	Yes. PC nos. 5, 7	✓	
35. A. Are noncurrent liabilities those whose liquidation is not expected to require the use of current assets or the creation of current liabilities? (B05)	Yes. PC nos. 5,7	✓	

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
B. If not, how are noncurrent liabilities defined?					
36. For notes payable, is disclosure made of: (C59 and Statement of Financial Accounting Concepts No. 5)					
a. Interest rates?	Yes. PC no. 5	✓			
b. Maturities?	Yes. PC no. 5	✓			
c. Assets pledged as collateral?	Yes. PC no. 5	✓			
d. Covenants to reduce debt?	Yes. PC no. 5	✓			
e. Minimum working capital requirements?	Yes. PC no. 5	✓			
f. Dividend restrictions?	Yes. PC no. 5	✓			
37. A. For long-term construction-type contracts, are the percentage-of-completion and completed-contract methods used? (CO4)	Yes. IAS no. 11	✓			
B. If so, what are the criteria for determining the method to be used?					37B. See IAS no. 11 and paragraph 79 of the text.
38. A. Are research costs charged to expense when incurred? (R50)	Yes. IAS no. 9	✓			
B. Are such costs disclosed?	Yes. IAS no. 9	✓			
39. A. Are development costs charged to expense when incurred? (R50)	Yes. IAS no. 9	✓			

B. Are such costs disclosed?	Yes. IAS no. 9	✓	
40. A. In the U.S., events and transactions are presented in the income statement as extraordinary items when they are unusual in nature and are of the type that would not reasonably be expected to recur in the foreseeable future. Do similar criteria for identifying extraordinary items exist in Italy? (I17)	Yes. PC no. 2	✓	
B. If not, what are the criteria?			
41. Are material events or transactions that are unusual in nature or expected to occur infrequently but not both (and thus do not meet the criteria for classification as extraordinary) shown as a separate component of income or expense? (I22)	Yes. PC no. 2	✓	
42. A. Are disclosures required for—			42A. In Italy, events that would not meet U.S. criteria for extraordinary items are treated as extraordinary.
a. Extraordinary items? (I17)	Yes. PC no. 2	✓	
b. Material events or transactions not classified as extraordinary items? (I22)	Yes. PC no. 2	✓	
c. Disposal of a segment of a business? (I13)	Yes. PC no. 2	✓	
B. Indicate the financial statement presentation of these items.			42B. Items *a* and *b* are usually illustrated on a separate line of the income statement. For item *c*, disclosure is not required in the income statement but *is* required in the notes.

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
43. A. Are pension costs provided for covered employees over the term of employment? (P15)	Yes. PC no. 7	✓			
B. If so, do they include charges for costs assigned under the actuarial method used to years prior to the plan's inception?	Yes. PC no. 7			✓	43B. Severence indemnities are unfunded, but not actualized by the actuary.
44. A. Are specific disclosures required relating to pension plans? (P15)	Yes. PC no. 7	✓			
B. If so, list them.					44B. Disclose entire pension liability.
45. A. When accounting income and taxable income differ, are deferred income taxes recorded for timing differences (as opposed to permanent differences)? (I24)	Yes. IAS no. 12		✓		
B. If so, are deferred taxes provided for all timing differences (as opposed to only those meeting certain criteria)?	Yes. IAS no. 12		✓		
C. If deferred taxes are provided only for those timing differences meeting certain criteria, what are the criteria?					
46. A. Are deferred taxes determined on the basis of tax rates in effect at the time the difference originated? (I24)	Yes. IAS no. 12		✓		46A. Deferred tax accounting generally not followed.

B. If not, on what basis?					
47. A. Is specific information related to income taxes required to be disclosed? (I28)	No		✓		47A,B. Disclosure is required if there is an unusual relation between income before taxes and income taxes. The reasons for the unusual relation are also to be disclosed.
B. If so, list the requirements.					
48. A. Are operating losses reported on the income tax return allowed to be carried backward to earlier periods? (I37)	No.			✓	48A. Loss carrybacks not allowed by law.
B. If so, are the tax effects of a loss carryforward included in the income in the period?					
49. A. Are operating losses reported on the income tax return allowed to be carried forward? (I37)	Yes. IAS no. 12	✓			
B. If so, are the tax effects of a loss carryforward included in the income in the period realized?	No	✓			
50. Are financial statements of a foreign entity prepared for consolidation purposes measured in the currency of the primary economic environment in which the entity operates? (F60)	Yes. IAS no. 21	✓			50. Foreign subsidiaries are translated at the current rate.
51. Are all elements of financial statements translated at current exchange rates? (F60)	Yes. IAS no. 21	✓			

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncement	Predominant Practice	Minority Practice	Not Done	Comments
52. A. Are translation adjustments reported separately? (F60)	Yes. IAS no. 21	✓			
B. Are they accumulated in a separate component of stockholders' equity until ultimately realized?	Yes. IAS no. 21	✓			
C. Is there an analysis of the changes during the period in the component of stockholders' equity relating to translation adjustments?	Yes. IAS no. 21	✓			
53. A. Are gains and losses resulting from transactions, denominated in a currency other than that of the environment in which the entity operates, included in determining net income for the period in which the exchange rate changes? (F60)	Yes. IAS no. 21	✓			53A,B. There is no Italian accounting standard yet issued concerning foreign currency translation and foreign currency transactions (one standard is in draft as of now). The Italian government has issued its own standards, which are being accepted temporarily by the profession. These standards require use of the current rate for receivables and payables in foreign currencies short-term, while for long-term assets and liabilities a variety of methods is acceptable, such as deferral of unrealized losses to be amortized on a systematic basis, historical rate if the use of the current rate
B. Is the aggregate transaction gain or loss included in determining net income for the period disclosed in the financial statements or notes?	Yes. IAS no. 21	✓			

				for long-term assets or liabilities would bring about an unrealized gain, or the charging of all unrealized gains and losses (long-term) to the income statement.
54. Are gains or losses on foreign currency transactions that are intended to hedge a foreign currency commitment deferred and included in the related transaction? (F60)	Yes. IAS no. 21		✓	
55. What information is disclosed about foreign currency restrictions?				55. Details of restrictions, items affected and effect on financial statements.
56. Are significant events arising subsequent to the balance sheet date reflected in the financial statements or notes thereto?	Yes. PC no. 7	✓		
57. Please list any standards for your country for which there are no corresponding U.S. standards.				57. None

Bibliography

The information in this booklet was compiled from many sources in Italy. Significant references follow.

- Auditing standards and accounting statements issued by the accounting profession
- Italian Civil Code
- Regulations of the Commissione Nazionale per le Società e la Borsa (Consob)

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