

## **Introduction of the two companies**

Carrefour is the world's second largest food retailer, and operates over 9,000 stores in 30 countries. Hypermarkets, supermarkets and hard discount stores are three major forms of business in Carrefour. In 2001, consolidated sales of Carrefour were € 69.5 billion (51% from international business), and net income from recurring operation was € 1.2 billion. Till the end of 2001, Carrefour had a total employee of 383,000 worldwide.

Safeway Inc. is one of the largest food and drug retailers in North America. Till the end of 2001, this company operated 1,773 stores in the United States and western Canada. The total sales of 2001 were \$34.3 billion. Safeway has extensive network of distribution, manufacturing and food processing facilities in order to support its stores.

Although Carrefour's turnover is approximate double of Safeway's, they both engage in food retail industry. Therefore Carrefour and Safeway Inc. is a matched pair of large quoted companies.

## **The different accounting regulatory environments in the U.S. and France**

### Legal systems

#### U.S.

The federal law of the United States generally is modeled on English common law. "A common law rule seeks to provide an answer to specific case rather than to formulate a general rule for the future". (Nobes C and Parker R, 2002) This naturally influences commercial law, which traditionally does not regulate the behaviour of companies and how they should prepare their financial statements. To a large extent, accounting within such a context does not depend upon law. Instead, accountants themselves establish rules for accounting practice, which may be written down as

recommendations or standards.

France

France has a codified law system, in which rules relate with justice and morality. They become doctrine. The accounting laws and decrees of the French state apply to all business enterprises, not just to companies. The keeping of accounting records and taxation report to owners and creditors as well. They include not only a Commercial Code but also a national accounting plan.

#### Accounting standards

U.S.

In the United States, accounting is regulated by the Financial Accounting Standards Board (FASB), which is a private sector body. However its standards are supported by the Securities and Exchange Commission (SEC), which is a governmental agency. Another private sector body, the American Institute of Certified Public Accountants (AICPA), is responsible for setting auditing standards. ‘Generally accepted accounting principles (GAAP) are the sum total of all financial accounting standards, rules, and regulations that must be observed in the preparation of financial reports’ (Choi F, Frost C and Meek G, 1999)

France

National uniform accounting system is advocate in France. The *Plan Comptable General* is general standards of accounts. The *Conseil National de la Comptabilite* (CNC) is attached to the Ministry of Finance. It is major responsible for keeping the Plan current and approving adaptations for specialized. The *Commission des Operations de Bourse* (COB) is equivalent to the SEC in US, but has important limited influence. The *Order des Experts-Comptables et des Comptables Agrées* (OECCA) is devoted to professional practice issues of accountants, and under the jurisdiction of the Ministry of Industry and Finance. The *Compagnie Nationale des Commissaires aux Comptes* (CNCC) is the professional association of independent

public auditors, and under the jurisdiction of the Ministry of Justice.

### Stock exchanges

U.S.

Zysman (1983) has formalized the type of financial system of the United States as capital market systems. In the U.S. shares of companies are held by millions of private shareholders and institutional investors. This kind of system is benefit to put pressure for disclosure, audit and 'fair' information, because of a widespread ownership of companies by shareholder who do not have access to internal information.

France

In Zysman's (1983) point of view, the financial system of France belongs to the credit based governmental systems. Capitals of most French companies are provided by banks, governments or founding families. The banks or the state will appoint directors and thus be able to obtain information and affect decisions. Meanwhile the need for published information is less clear. This also applies audit, because this is designed to check up on the managers in cases where the owners are outsiders. However the auditing profession in France is not as large as in U.S.

### **Classification study between the U.S. and France**

Muller (1967) classified the accounting system of the United States as an independent discipline. This sort of system is highly independent from governments or economic theories. In this type of system, theory is not so respected, but in emergencies or used ex post to justify practical results. 'General accepted accounting principles' are typical expressions. Nobes (1984) classified the US accounting system as micro-based, business practice, pragmatic, British origin. Through Nobes' classification, the US accounting system is independent, individual basis, practical basis, and came from British model.

France was classified as uniform accounting by Muller (1967). In such system, accounting has been used as a tool of the administrative control of business by governments. Measuring performance, allocating funds, assessing the size of industries and resources, controlling prices, collecting taxation, manipulating sectors of business are using accounting as a tool. Standardization of definitions, measurements and presentation are involved in this system. Nobes also got similar classification for France. By Nobes (1984) the French accounting system was classified as Macro-uniform, government, and tax-based, legal system. The French accounting system is doctrinal, and influenced by government a lot.

### **Comparison of main accounting measurement techniques**

Carrefour and its international subsidiaries prepared the consolidated financial statements accordance with French accounting principles. The accounting principles used by Carrefour also comply with US GAAP except for several aspects. Therefore the differences of accounting measurement techniques applied by Carrefour and Safeway Inc. are not very obvious. However, there still are some differences, which are described as follows:

#### **□ Inventories**

In Carrefour inventories of merchandise are valued at the last purchase price plus any related costs, a method suitable for rapid inventory rotation. Safeway Inc. adopts a last-in, first-out (“LIFO”) basis or market value on \$1,906 million of merchandise inventories at year-end 2001. All remaining inventory is valued at the lower cost on a first-in, first-out (“FIFO”) basis or market value. The FIFO cost of inventory approximates replacement or current cost. Compared with Safeway Inc., Carrefour has a more flexible method to value inventories. However, Safeway Inc. is using more conservative methods than Carrefour. LIFO is popular in US because it can be used for federal income tax purpose. Furthermore, if LIFO is used for tax purposes, it must also be used for financial reporting purposes.

#### □ Depreciation

In both of these two companies, land, building and improvement and equipment are valued at their original cost price, and depreciation is calculated by same method, the straight-line method based on average life. However, in Carrefour lives of buildings are 20 years, the same things of Safeway Inc. are 7 to 40 years. Safeway Inc. uses the lives of 3-15 years for fixtures and equipment. Nevertheless in Carrefour they are 8 and 6 years separately. According to the comparison, Safeway Inc. estimated much longer useful economic lives of assets than Carrefour. It means Safeway Inc. adopts more conservative accounting policies than Carrefour, because the length of depreciation influences straight how much tax the company should pay in these years. Therefore, it might affect the company's performance of these years, and the judgment of investors. In France tax laws rule allowable amounts of depreciation and amortization, however they are not always related to actual costs. Therefore the depreciation policies of Carrefour have been regulated generally.

#### □ Income tax

Safeway Inc. provides a deferred tax expense or equal to the change in the deferred tax liability during the year in accordance with Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for Income Taxes." For both Safeway Inc. and Carrefour, deferred income taxes represent tax credit carry-forwards and future net tax effects due to temporary differences between the financial statement and tax basis of assets and liabilities that are calculated at the tax rate in effect at the beginning of the following year. Meanwhile these differences are expected to reverse in Safeway Inc.'s accounting policy. In Carrefour deferred tax assets and liabilities are discounted if the impact of discounting is significant. The rate used to value deferred taxes in France reflects the impact of any additional taxes paid. There is a divergence between income for commercial accounting purposes and income for tax purposes, therefore deferred tax accounting is rarely found in the individual accounts of French companies.

### **Comparison of corporate governance**

Safeway Inc. adopts the typical Anglo-American Board structure. The Board of Directors of Safeway Inc. consists of 9 members, including 6 independent directors who hold a position in other organizations or just invest as private investors. Steven A. Burd is Chairman, President and Chief Executive Officer. There is an Audit Committee, which is composed entirely of outside directors in Safeway Inc. In Safeway Inc.'s annual report of 2001, there is not much information about corporate governance. The disclosure of this aspect is further not enough. However, it still represented obvious characteristics of the US system. The CEO is also the chairman and the President at the same time. Combining the two positions will give the CEO, who is also the chairman, opportunities to manipulate his board. Nevertheless it good to avoid the conflict between Chairman and CEO, and the leader can intimately involve in the business. In the Board of Directors, majority is independent outside directors. This gives them a structure that makes possible for them to monitor more effectively. It also brings some benefits to companies such as good reputation, new investment, and good relationship with business partners etc., because generally the independent outside directors almost hold important positions in other corporations, which might be business partners, or they own good reputation in society.

The states or families always control French companies. Carrefour is also not an exception. Halley Family Group, the biggest shareholder of Carrefour, owns 11.51% shares. Daniel Bernard is the Chairman-Chief Executive Officer of Carrefour. The Board of Directors of Carrefour is 'made up of 11 numbers, including 3 independent directors who do not hold a position and have never held a position within the company or any of its subsidiaries. Each director must own at least 600 shares during his six-year term of office. The Board of Directors met six times in 2001 with a 91% attendance rate for all directors.' The Board of Directors has 3 specialized committees. The members are all from Board members. Their duties are to study certain specific issues and to report to the Board of Directors. These three committees are strategic

orientation committee, audit committee and compensation committee. The Strategic Orientation Committee is responsible for making the decisions that are most important for the future of the Group. It met twice in 2001. The Audit Committee is mainly charge of reviewing the parent company and consolidated financial statements. It met three times in 2001. The Compensation Committee proposes the compensation of corporate officers. It met once in 2001. In Carrefour's annual report of 2001, there is detailed information about the work of the Board of Directors and compensation of officers etc. The disclosure of information of Carrefour is plenteous under French law. Comparison between these two companies, corporate governance does not have obvious differences. Carrefour uses the similar system with Anglo-American Boards structure. However in the Board of Directors minor members are independent outside directors.

### **Assessment of the foreign currency translation and segmental reporting disclosures**

In the US, foreign currency translation follows the requirements of SFAS 52. The new standard is based on the concept of "functional currency", which means "the currency of the primary economic environment in which the company operates." (Lawrence S, 1996) Safeway Inc. chooses local currency as their functional currency for their foreign subsidiaries. This can be seen on the description of the Safeway Inc.'s annual report, "Assets and liabilities of the Company's Canadian subsidiaries and Casa Ley are translated into U.S. dollars at year-end rates of exchange, and income and expenses are translated at average rates during the year. Adjustments resulting from translating financial statements into U.S. dollars are reported, net of applicable income taxes, as a separate component of comprehensive income in the consolidated statements of stockholders' equity". The disclosure of Safeway Inc.'s foreign currency translation policy is accurate and clear. For expediency, average exchange rates are used for income and expenses items. Normally, closing rates could be adopted as well.

More than 98% of consolidated sale of Safeway Inc operates in the United States and Canada. Safeway's retail grocery business is its only reportable segment. In its annual report a geographical segment report is presented. In US, the SFAS 14 'Financial Reporting for Segments of a Business Enterprise' should be followed when a company produces a segment report. According to comparison between Safeway's segment report and the SFAS 14, this segment report has reached the requirement of the standard. The disclosure of information has achieved the basic level of requirement. If it showed more details about depreciation charged, capital expenditure, types of products and services supplied and income from enterprise accounted for using the equity method, information might be disclosed more sufficiently.

Carrefour separates its foreign currency translation policy into two parts. One is for its subsidiaries doing business in high inflation countries. In this situation 'non-monetary items are revalued based upon the decline in general purchasing power of the local currency during the year. All balance sheet items are converted into euros based upon the rates in effect at year-end. The statement of income in local currency is adjusted for inflation between the transaction date and the end of the year. All items are converted based upon the rates in effect at year-end.' For other companies, 'balance sheet items are converted by same principles, just without prior restatement for the effects of inflation. And income statement items in local currency are converted at the average rate for the year, weighted to take into account each company's seasonal business.' Carrefour also adopts local currency for its oversea subsidiaries as their functional currency. More conservative policies are chose by this company because it is doing business in variable and complicated situation and large number of countries. Compare with Carrefour, Safeway Inc. is enjoying its stable situation. Carrefour chooses both the temporal and the closing rate method to translate the financial statements of oversea subsidiaries. The use of these two methods depends on how foreign entity is closely linked to the French parent.



There are no formal segment reports in Carrefour's annual report. But some analyses by geographic region are still available. The relevant information is just about sales net of taxes, EBITDA (earning before interest, tax, depreciation and amortization) and EBIT (earning before interest and tax) before goodwill. Therefore some big differences about segment reporting between Carrefour and Safeway Inc. the main reason might be that different organizations have different structure of the group. Hence there will certainly be different between segment reporting in different organizations in different countries. If there was sufficient information about assets, depreciation and capital etc., it should be more helpful for investors, analysts, and accounting and securities markets regulators.

### **Calculation and analysis of eight key accounting ratios**

#### □ Return on capital employed (ROCE)

This ratio of Safeway Inc. was 19.1% in 2001. Carrefour's was 13.8%. It seems that Safeway Inc. got better effectiveness in deploying funds. At the same time Safeway got more satisfied return back from investment. In 2000 Safeway Inc.'s ROCE was 18.7%. In that year the ROCE of Carrefour was 14.6%. According to comparison with 2000, Safeway Inc. kept stable performance. In 2001 Carrefour got a little bit lower return on capital employed than 2000 fiscal year, although its current liabilities were reduced over the year. Generally Safeway Inc. had better overall performance comparing with Carrefour.

#### □ Net profit margin

Safeway Inc.'s net profit margin of 2001 was 7.5%. Carrefour's was 4.1%. In 2000, this ratio of Safeway Inc. and Carrefour are 7.1% and 4.2% separately. Both these two companies had low profit margins because of their industry. They both kept their stable net profit margin. Compare with Carrefour, Safeway Inc. got better operational performance on these figures. This might be influenced by the company's marketing strategy. Carrefour owns many hard discount stores, which maybe affect the profit.

#### □ Gross profit margin

In 2001 Carrefour's gross profit margin was 22.5%. Safeway Inc. had a better figure on this ratio; it was about 8.4% higher than Carrefour. In 2000, these figures were 29.7% and 23.1% for Safeway Inc. and Carrefour separately. Large amount cost of sells of Carrefour is the reason due to the vast size of Carrefour.

□ Average stock turnover period

Average stock turnover period of Safeway Inc. was 39 days. Carrefour's was 39 days as well. Their inventories were turned over every 39 days. Especially a supermarket chain should prefer a low stock turnover period, because funds cannot be used for other profitable purpose if they are tied up in stocks.

□ Current ratio

Safeway Inc.'s current ratio was 0.85 times. The same ratio of Carrefour was 0.75 times. As a supermarket chain this ratio should be as lower as better. Carrefour has got much lower current ratio than Safeway Inc. It will be helpful to hold only fast-moving stocks of finishing goods and generate mostly cash sales. The average current ratio was approximate 1.38 times for 1996 for UK listed companies operating in consumer goods industrial sectors. (McLaney E and Atrill P, 1999) They were both below than 1.0, which means the liquid assets cannot cover the current liabilities. It might cause some liquidity problems.

□ Acid test ratio

In fiscal year of 2001 Safeway's acid test ratio was 0.19 times, same with the year of 2000, and Carrefour's was 0.68 times, 0.12 higher than in 2000. Compare between current ratio and acid test ratio, Safeway Inc. held much more stocks compared with Carrefour in their current assets. It might be risky because the stock in hand cannot be converted into cash quickly.

□ Interest cover ratio

In 2001 this ratio of Safeway Inc. was 5.79 times. And for Carrefour interest cover ratio was 4.37 times. Compare between these two ratios, Safeway Inc. had higher level of profit coverage for interest expense than Carrefour. Therefore for the lenders of Safeway Inc. they got lower level of risk. However, 3.86 times is the interest cover ratio for Carrefour in 2000, which means in 2001 Carrefour has make some

adjustment to reduce the risk for its lenders.

#### □ Earning per share (EPS)

Earning per share of Safeway Inc. was \$2.49 in 2001. This figure increased \$0.30 comparing with 2000. In 2001 the figure of Carrefour was €2.21. EPS of Carrefour was €1.94 in fiscal year of 2000. This is a fundamental measure of share performance. The trend in EPS is used to help assess the investment potential of a company's shares. Therefore, both these two companies' performance is pretty good within these two years.

From the figures, Safeway Inc. had better financial performance in 2001 generally. However it still should pay more attention on improving the current ratio, and controlling the quantity of their held stocks. Furthermore figures cannot mean everything. Carrefour is still doing successful business. Huge size might be the main problem for Carrefour. It has to face more complicated and variable global economic and market environment. The target market for Safeway Inc. is only the North America, which means the problems might be comparatively simple.

### **Conclusion**

After comparison of general regulation environments, classifications, accounting measurement techniques, corporate governance, the foreign translation and segmental reporting disclosures and ratios between Carrefour and Safeway Inc., there are several obvious differences. The outside reasons mainly are different regulation environments and different corporate governance systems. The inside reasons are that the two companies adopt different degree of conservatism and the different degree of disclosure for different types of information. In general, it would be better that Safeway Inc. put more detailed information about corporate governance, not just the list of the Board of Directors. It also will be helpful that Carrefour can give more details about its segmental report. Whether they are in which systems, there are advantages and disadvantages. Exploit its favourable conditions and avoid

unfavourable ones is the key principle to success.

## Appendix

Return on capital employed (ROCE)=  

$$\frac{\text{Net profit before interest and taxation}}{\text{Share capital + Reserves + Long -term loans}} \times 100$$

Net profit margin=  

$$\frac{\text{Net profit before interest and taxation}}{\text{Sales}} \times 100$$

Gross profit margin=  

$$\frac{\text{Gross profit}}{\text{Sales}} \times 100$$

Average stock turnover period=  

$$\frac{\text{Average stock held}}{\text{Cost of sales}} \times 365 \text{days}$$

Current ratio=  

$$\frac{\text{Current assets}}{\text{Current liabilities}}$$

Acid test ratio=  

$$\frac{\text{Current assets (excluding stock)}}{\text{Current liabilities}}$$

Interest cover ratio=  

$$\frac{\text{Profit before interest and taxation}}{\text{Interest payable}}$$

Earnings per share (EPS) =  

$$\frac{\text{Earnings available to ordinary shareholders}}{\text{No. of ordinary shares in issue}}$$

## Reference

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