



**IFRS:
GLOBAL RULES &
LOCAL USE**

Prague, October 18, 2013

Anglo-American University, Prague – Czech Republic

**PROCEEDINGS OF THE 1ST INTERNATIONAL
SCIENTIFIC CONFERENCE**

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Introduction

These proceedings are published to accompany the **1st year of the international scientific conference** entitled **IFRS: Global Rules and Local Use**, taking place on October 18, 2013 at the Anglo-American University in Prague.

The proceedings contain contributions prepared and authored by conference participants and presented during the conference. The contributions were reviewed and accepted by the editorial team and group of external reviewers.

Papers and abstracts are thematically divided into sections:

- Plenary session I – Academics
- Plenary session II – Professional Accountants and Auditors
- Parallel section I – Financial reporting issues and IFRS adoption
- Parallel section II – IFRS adoption, cultural differences and ethical issues

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IFRS – ONE SIZE FITS ALL?

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Abstract: *This presentation will be loosely based on, but developed as the mood takes from, ideas briefly summarised in Alexander (2012). The essential point is that accounting, like in fact most things, is a social construction. A fair presentation is one which is perceived as fair by a particular person, at a particular time, in a particular place, for a particular purpose. Financial reporting, construed broadly as the process of attempting accountability to stakeholders, has a variety of different user types, with a variety of different decisions to take. Sources of finance are one, but only one, of the significant factors likely to be involved. Different country scenarios have different balances between the various needs, and this has implications for the notion of global harmonisation (note that the British and the Americans cannot even harmonise the spelling of the word harmonize....). Full IFRS, as now adopted for consolidated financial statements of listed groups, have a specifically stated, and quite narrow, suppliers of finance ‘objective’, as paragraphs OB 2 and OB 10 of the 2010 Framework make clear.*

In particular, the size and degree of complexity of the reporting entity is likely to be important. ‘SME’ covers a wide range of sizes, from the very small to the not quite large, and cases must be considered on their individual merits. But as a generalisation the greater the relative importance of tax and dividend calculation, creditor (especially bank) protection, family (insider) finance and management, and so on, as compared with providers of external, in principle international, finance, the less logical it becomes to expect, let alone find the existence of, suitability of IFRS for SME reporting.

As a framework to the presentations and discussions of the day, some implications are suggested.

REFERENCE

Alexander D. (2012). Is there such a thing as European Financial Reporting? Financial Reporting vol. 4 No. 4 pp 7–13.

WHAT ABOUT PRUDENCE?

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Abstract: *In July, the IASB issued its Discussion Paper (DP) on the Conceptual Framework. However, the IASB does not intend to fundamentally reconsider the content of Chapter 3 The Qualitative Characteristics of Useful Financial Information of the existing Conceptual Framework issued in 2010. The IASB will make changes to those chapters if work on the rest of the Conceptual Framework highlights areas that need clarifying. The DP also discusses the concerns that some have raised with how these chapters deal with the issues of stewardship, reliability and prudence. What about prudence? I briefly look at the evolution of the concept of prudence in accounting, present some research on the impact of IFRS on prudence (e.g., André, Filip and Paugam, 2013) and debate whether or not it should be part of the Conceptual Framework.*

Keywords: *Conceptual Framework, IASB, prudence, qualitative characteristics, reliability, stewardship*

PROPERTY, PLANT AND EQUIPMENT VALUATION IN THE FINANCIAL STATEMENT OF COMPANY AT BANKRUPTCY RISK IN POLAND

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Abstract: *The major objective of financial statements in entities which continue their business activity is to satisfy information needs of wide range of users and to lower the economic and investment risks in competitive business environment of countries, regions and the world. Adopting the assumption to discontinue operation influences the assets valuation of a given entity.*

Property valuation is one of the key elements of bankruptcy proceedings, as its accuracy affects whether the court examines or dismisses the petition and what type of proceedings it orders. The stage of verification whether it is possible to go through with bankruptcy proceedings bears consequences for the parties and it may possibly have social consequences as well.

Information regarding value of fixed assets is extracted from the balance sheet and on the basis of estimated property valuation.

The paper objective is to present principles of property, plant and equipment valuation in conditions of bankruptcy risk. Differences in property, plant and equipment valuation in accordance to the Polish Accounting Act and IFRS will be discussed, along with the impact of legal regulations on credibility of information presented in proceedings documentation for a bankruptcy declaration conducted in Poland.

In order to accomplish the objective, the research method was used consisting of:

- *literature studies, with particular emphasis on the legal basis for property valuation of an enterprise at bankruptcy risk,*
- *empirical studies carried out on a group of 100 companies on which courts declared bankruptcy in 2011. The study sample constitutes 14% of the population and is a significant representation of the phenomenon in Poland.*

Keywords: *bankruptcy, fixed assets, Poland, valuation*

1. INTRODUCTION

One of the most important issues related to the economic activity of an enterprise is a reliable valuation of assets and presentation of their value in the financial statements. The asset valuation is also important in case of a threat of bankruptcy. It is one of the key elements of bankruptcy proceedings.

An entity's ability to continue as a going concern or a substantial doubt about an entity's ability to continue as a going concern will affect the asset valuation scheme. This assumption will be reflected in the entity's financial statements. The balance sheet of the company at bankruptcy risk is one of the documents filed with the court in bankruptcy proceedings. The court obtains the information on the value of the debtor's property from the balance sheet and from the estimated value of the property.

The information obtained in the initial phase of bankruptcy proceedings determines the choice of proceedings. Based on the information about the debtor's property, the court decides whether the company is able to bear the costs of bankruptcy proceedings. The court also

determines whether the enterprise is able to better satisfy the creditors' claims by liquidation of the debtor's assets or by entering into an arrangement with creditors. One of the assets that can be sold to satisfy the creditors' claims in bankruptcy proceedings is property, plant and equipment. Therefore, the information on the value of property, plant and equipment of the insolvent debtor in bankruptcy proceedings may influence whether the court accepts or dismisses the petition to declare bankruptcy and the choice of proceedings.

Deliberations contained in this study are based on the belief that the financial statements of an economic entity, at any stage of its operation, should provide reliable and trustworthy information on the value of its assets. Legal regulations in the field of accounting determine the scope of information contained in the financial statements. In addition, in bankruptcy proceedings, the relevance of information resulting from the financial statements depends on the rules laying down the debtor's reporting requirements.

The paper objective is to present principles of property, plant and equipment valuation in conditions of bankruptcy risk. Differences in property, plant and equipment valuation in accordance to the Polish Act on Accounting and IFRS will be discussed, along with the impact of legal regulations on credibility of information presented in proceedings documentation for a bankruptcy declaration conducted in Poland.

In order to accomplish the objective, the research method was used consisting of:

- literature studies, with particular emphasis on the legal basis for property valuation of an enterprise at bankruptcy risk,
- empirical studies carried out on a group of 100 companies on which courts declared bankruptcy in 2011. The study sample constitutes 14% of the population and is a significant representation of the phenomenon in Poland.

2. EUROPEAN UNION REGULATIONS CONCERNING CROSS-BORDER INSOLVENCY PROCEEDINGS

Insolvency law is an important part of legal framework of economies. Transparent insolvency regulations give investors confidence. In most of the more developed legal systems, insolvency law has grown in importance, but countries continue to look for the best bankruptcy solutions. (Wessels, Markell, Kilborn, 2009, p. 1–2)

The enlargement of the European Union and the accompanying globalization result in the fact that the activities of undertakings go beyond the borders of one country more and more frequently and, as a consequence, they are subject to the provisions of community law. Efficient functioning of the European Union internal market requires efficient legal solutions in many areas, including cross-border insolvency proceedings. (Bauer, 2010, p. 177–178)

In order to ensure efficient insolvency proceedings, the Council Regulation (CE) no. 1346/2000 on insolvency proceedings was adopted on May 29, 2000. This regulation entered into effect on May 21, 2002. (Feber, 2004, p. 10) It applies to all insolvency proceedings regardless from the fact whether a debtor is a natural person, a legal person, a trader, or an individual, excluding insurance undertakings, credit institutions, investment undertakings which provide services involving the holding of funds or securities for third parties, and collective investment undertakings. The Regulation on insolvency proceedings applies only in cases when the centre of the debtor's main interest is situated within the Community.

The centre of the debtor's main interest is the place in which the debtor conducts the administration of his interests. Pursuant to the Regulation, main insolvency proceedings as well as secondary insolvency proceedings may be initiated. Main insolvency proceedings is instituted within the territory of the Member State in which the centre of the debtor's main interest is situated. Apart from the main proceedings, secondary proceedings may be initiated in states in which the debtor has his establishments. The main proceedings encompasses the whole property

of the debtor; the secondary proceedings covers only the assets situated in the state of the secondary proceedings. (Council Regulation (CE) no. 1346/2000, 2000)

In conclusion, Council Regulation (CE) no. 1346/2000 on insolvency proceedings provides only for jurisdiction, that is to say it specifies which Member State may open insolvency proceedings. Each Member State has its own separate legislation concerning insolvency proceedings. This means that types of insolvency proceedings and ways of liquidation depend on the place in which the proceedings is conducted. On account of globalisation, growing international exchange concerning all aspects of economic life, and the transfer of financial difficulties between states, it seems important to become acquainted with insolvency regulations of individual Member States. Regulations in the state of the insolvency proceedings will influence the efficiency of the proceedings from the point of view of creditors as well as debtors.

Regulations on accounting, including also the valuation of assets of the company at bankruptcy risk, will influence the efficiency of the bankruptcy proceedings as well.

Polish accession to the European Union took place on 1 May 2004. It resulted in the free flow of goods, services, capital, and labour force and had an impact on the legislation, including bankruptcy proceedings and accounting.

3. ESSENCE AND SPECIFICITY OF BANKRUPTCY PROCEEDINGS IN POLAND

Bankruptcy of enterprises is generally recognized as a negative phenomenon. It results from serious financial problems of an enterprise; its consequences may affect other economic entities. Declaration of bankruptcy influences employees and contractors of a bankrupt party. It is connected with a loss incurred by creditors as well as by the owners of a bankrupt company.

In practice, the institution of bankruptcy aims at protecting interests of market game participants. It eliminates from the market the enterprises which are not able to conduct their activities effectively. This way, it also protects other entities from establishing relationships with a company which is unable to rival its competitors.

The issue of bankruptcy may be discussed in its legal as well as economic aspect. Economic bankruptcy does not always mean legal bankruptcy. On the other hand, each bankruptcy declared by the court means economic bankruptcy. Pursuant to the law, an undertaking is bankrupt after the court has declared it bankrupt. But, from the economic point of view, a bankrupt is an undertaking which is not able to fulfil its obligations on time and the value of its assets is not enough to cover its liabilities even if the undertaking in question still conducts its activities.

In Poland, bankruptcy of undertakings is regulated by the Act as of February 28, 2003 *The Law on Bankruptcy and Reorganization* (LBR). This law applies to entrepreneurs and – from 2009 – to natural persons not conducting economic activity, who became insolvent due to exceptional circumstances not attributable to them as well.

The legislator in Poland has provided for the following possibilities in the case of financial problems:

- bankruptcy by liquidation of the debtor's assets,
- bankruptcy with a possibility to make an arrangement,
- reorganization proceedings.

The first two types relate to bankruptcy proceedings. Reorganization proceedings applies in the case when a debtor has no grounds to apply for the declaration of bankruptcy; however, in his opinion, the financial condition of the undertaking indicates that in the foreseeable future the undertaking is at bankruptcy risk and the debtor wants to prevent it.

The Bankruptcy and Reorganization Law introduced a series of concepts and mechanisms to Polish law and business practice as well. The purpose of these changes was to accelerate the bankruptcy proceedings and to make them more flexible.

Bankruptcy is the result of economic problems. The grounds for declaring bankruptcy are formed by the fact that a debtor does not pay its due liabilities. A debtor is also recognized as insolvent (which means he may be declared bankrupt) in the case when the total value of his obligations exceeds the value of his assets even if he pays his obligations on time. (LBR, 2003)

Causes of enterprise bankruptcy are different in different countries. This may be a result of the level of economy development in a given country, legislation, experience in examining enterprise bankruptcy, and early detection of symptoms of approaching crises. (Bauer, 2009, p. 13)

In practice insolvency, risk and bankruptcy issues are not sufficiently recognized. Whereas studies identifying threats to company operations may be an important factor for business development enterprise theory and business practice rationalization (Mączyńska, 2009, p. 19–23). Research of company bankruptcy is largely focused on forecasting company insolvency, while the subject of bankruptcy proceedings as an economic process is tackled extremely rarely.

Since insolvency is a social problem attempts towards reducing the number of bankrupting companies has great significance for economies. Bankruptcy declaration is to protect the market players by eliminating from the market companies which are unable to match their competitors. The key objective of bankruptcy proceedings is to protect creditors' interests, that is to settle their accounts to the greatest possible extent, ideally completely. However, should the company encounter only temporary difficulties possible to overcome by entering and executing an agreement more beneficial for the creditors than repayment of draws from realisation of the liquidation proceeds, the court does not deprive the indebted company of the possibility to continue its business activity. Restructuring process may be implemented as bankruptcy with possibility to make an arrangement or reorganization proceedings. Reorganization proceedings is in practice initiated very rarely, while the bankruptcy with possibility to make an arrangement constitutes more than a dozen of all bankruptcy proceedings in Poland.

4. THE ROLE OF PROPERTY, PLANT AND EQUIPMENT IN CASE OF A SUBSTANTIAL DOUBT ABOUT AN ENTITY'S ABILITY TO CONTINUE AS A GOING CONCERN

Changes in the economic environment, such as the development of information and communication technologies and globalization result in enterprises facing new challenges. The pursuit for improving the quality of human life, protecting the environment and ensuring the clarity and transparency of business activities deserves our special attention. These changes cause the growing importance of intangible assets in the process of building competitive advantage. (Paliwoda-Matiolańska, 2009, p. 168–169).

The approach to an enterprise's assets changes, however, if there is a substantial doubt about an entity's ability to continue as a going concern. In case of liquidation of an enterprise in bankruptcy proceedings, the assets that can be sold will be of essential significance. The money from the sale will be used to repay debts.

The court uses the information about the value of the debtor's property at the initial stage of bankruptcy proceedings. This information is derived from the balance sheet and from the list of items of property, with the estimated valuation of assets, that the debtor has filed with the petition to declare bankruptcy; and then from the value estimate of property made by an interim court supervisor (if appointed). The value of the property is the basis for deciding whether the debtor is able to cover the costs of bankruptcy proceedings and which type of proceedings will better satisfy the creditors' claims.

In every type of bankruptcy proceedings, the primary objective of authorized legal representatives is to satisfy the claims of creditors to the fullest extent possible, preferably in full. The realization of this task will be, however, completely different and will result in a different approach to individual assets of a debtor, including property, plant and equipment, in bankruptcy proceedings by liquidation of the debtor's assets or bankruptcy proceedings with a possibility to make an arrangement.

For business units continuing as a going concern and making the balance sheet valuation, it is a prerequisite for the reliability of estimates to determine the future economic gains of a given entity and its assets, i.e. to determine its commercial value and its use value. The use value requires establishing all the evidence in order to determine objectively the ability to bring gains in the event of continuing business activity, while the commercial value requires determining economic gains in the event of sale (Karmańska, 2008, p. 332–334).

Similarly, in the bankruptcy proceedings, the court and the court-appointed representatives have the task of estimating the economic gains from the sale of the company or from continuing as a going concern by an entity at bankruptcy risk. The main difference lies in assuming that:

- possible sale will take place in conditions of forced sale,
- an entity at bankruptcy risk, while continuing as a going concern, may not bring such profits as would be generated by an enterprise not having financial problems confirmed by a petition to declare bankruptcy.

These assumptions further jeopardize the estimates of use value and of commercial value of an enterprise threatened with bankruptcy and its individual assets.

In the event of bankruptcy proceedings leading to the liquidation of the insolvent debtor's assets, the creditors' claims can be satisfied by selling the company, its organized parts or all the assets that have a so-called "selling value", i.e. the realizable value in case of forced sale. In the event of bankruptcy proceedings with a possibility to make an arrangement, the company continues as a going concern, and its assets are allowed to generate profits that will serve to repay the debts.

Accordingly, in the event of liquidation what is vital is the commercial value that can be derived from the sale of property, plant and equipment, while in the proceedings for an arrangement with creditors – what counts is the ability to generate revenues. It should be emphasized, however, that in both cases, this value is mainly important in the context of satisfying creditors' claims.

It is in the interest of the debtor who wants to continue his economic activities to demonstrate that the value of his assets is sufficient to open bankruptcy proceedings. However, in case of forced sale in the bankruptcy proceedings by liquidation of the debtor's assets, the creditors' claims will be satisfied to a lesser extent than through revenues derived from continuing business operations. Asset valuation made by debtors shall be verified by representatives of the court.

To sum up, the debtor shall be guided by the intention of disclosing in the balance sheet the value of each asset in accordance with the balance sheet law. However, in the current list of items of property with the estimated valuation, the debtor shall be guided by the intention of determining the value that can be obtained in case of forced sale.

5. FINANCIAL REPORTING IN PROCEEDINGS ON DECLARING BANKRUPTCY

Enterprises of the global economy have to adapt to the evolving market expectations in terms of information provided to users of financial statements. On the other hand, still developing accounting rules become a challenge for the average entrepreneur's abilities. (Świetla, 2013, p. 995, 1007)

Each country has its specific accounting system. The system of a given country has been shaped by its historical, cultural and religious conditions, and by events and processes that the country has experienced. In times of globalisation differences occurring between the national accounting systems make communication more difficult. However, creating one international accounting system based on one set of notions, rules, regulations and procedures is virtually impossible. (Krasodomska, 2010, p. 119, 134) The evolution of the Polish accounting system may lead to a belief that this system does not differ much from the solutions adopted in the International Financial Reporting Standards (IFRS). Applying IFRS in Poland may have a positive impact on the quality of financial statements. IFRS regulates some legal areas which have not been regulated in the Polish Accounting Act. In addition, IFRS have extended the scope of existing legislation. However, IFRS are applied by only a small number of entities in Poland (Grabiński, Kędzior, 2005, p. 266, 274).

Understanding and interpreting information coming from enterprises' book accounts requires having knowledge of regulations existing in a given country.

One of the tasks of accounting in enterprises is a reliable valuation of assets. Their valuation is influenced by legal regulations on accounting which exist in a given country. Another basic issue is also access to information from book accounts which results from the requirement of keeping book accounts and publishing financial statements.

The reporting obligations applying to a debtor in bankruptcy proceedings are regulated by the Act on Bankruptcy and Rehabilitation, and the rules for valuation of assets – by the Accounting Act.

The bankruptcy proceedings consist of two main stages i.e. the initial proceedings on declaring bankruptcy, when the court takes a decision on the possibility of declaring bankruptcy, and the actual proceedings after the court has declared bankruptcy. Already at the initial stage, at the start of bankruptcy proceedings, the court makes a decision based on the analysis of information concerning the valuation of the debtor's property, including the information from the debtor's balance sheet.

The major objective of financial statements in entities which continue their business activity is to satisfy information needs of wide range of users and to lower the economic and investment risks in competitive business environment of countries, regions and the world. (Surdykowska, 1999, p. 24). The role of an accountant is to create a financial statement which allows measure the performance of a company and help assess its current financial position. Reliable financial statements are essential for the proper functioning of financial markets. Therefore, large EU companies prepare their financial statements according to IFRS. (Klimczak, Mulenga, 2009, p. 427) However, measurements performed in the enterprises' accounting are not fully objective (Surdykowska, 2012, p. 105). Methods of determining the fair value of assets could be controversial. (Newton, 2010, p. 136) Some research and studies conducted in enterprises in Poland on legal regulations concerning balance sheets have shown that the picture of an enterprise's financial results presented in book accounts is usually reliable from the point of view of the existing accounting regulations. However, a comparison of this picture with economic reality raises doubts or even diverges broadly from the economic truth. (Mączyńska, 2009, p. 51)

The provisions of the Act on Bankruptcy and Rehabilitation currently existing in Poland limit the parts of financial statements required to be submitted together with the petition to declare bankruptcy only to the balance sheet – prepared no later than 30 days before the petition to declare bankruptcy is submitted – and in case of debtors who submit petition to declare bankruptcy with a possibility to make an arrangement – the cash flow statement for the last 12 months (Act on Bankruptcy and Rehabilitation, Art. 23). However, if the debtor proves that he is not able to enclose the required documents to his petition, he is released from this obligation.

Balance sheet, which is the oldest and still the most important part of financial statement, is treated as a “snapshot” of an enterprise, presenting a “true picture” of the enterprise's financial

situation on a given day (Wędzki, 2009, p. 51). In proceedings on declaring bankruptcy it is usually the only part of financial statement enclosed in the court case file. The issue of whether a balance sheet of an entity threatened with bankruptcy can be in fact, without any additional information, a reliable picture of the enterprise's economic position remains problematic.

A financial statement, in this case a balance sheet, is drawn up in order to present to its recipients useful information on the economic position, financial standing and achieved financial result of an enterprise. Therefore, it is in the interest of the recipients to know the principles based on which it was drafted. In practice, adopting an assumption of the enterprise not being able to continue as a going concern influences the valuation of the entity's assets. Information on whether a statement was drafted with the “going concern” assumption or “not a going concern” assumption is included in the introduction to the financial statement (Wielgórska– Leszczyńska, 2012, p. 621–623). Such additional information in economic practice is a source of information important for understanding a financial statement, also with regard to methods of valuation and methods of drafting the statement to the extent to which an enterprise has the right of choice guaranteed by statutory law.

The provisions of the Act on Bankruptcy and Rehabilitation recommend submitting the debtor's balance sheet without additional information, therefore depriving its recipients of the information on whether it was drafted with “going concern” assumption or not. Therefore, a balance sheet in the proceedings on declaring bankruptcy has a limited informational value as far as the adopted principles of valuing the debtor's assets.

6. VALUATION OF PROPERTY, PLANT AND EQUIPMENT IN THE FINANCIAL STATEMENTS OF AN ENTITY AT BANKRUPTCY RISK

According to the Polish Accounting Act, property, plant and equipment this is “tangible fixed assets and their equivalents, with an expected useful economic life longer than one year, complete, fit for use and designed to serve and undertaking's purposes. They include in particular:

- immovable property – including land, the perpetual usufruct right to land, buildings and structures, as well as premises owned on a separate basis, cooperative ownership rights to residential premises, and cooperative rights to commercial premises,
- plant and machinery, means of transport and other things,
- improvements in third party items of property, plant and equipment,
- livestock.” (The Accounting Act, p. 11)

Items of property, plant and equipment classified as fixed assets in the course of their construction, assembly or in the course of improvement of an existing item of property, plant and equipment are called construction in progress. (The Accounting Act, p. 13)

The enterprises which draw up financial statements in accordance with the Polish Accounting Act, assuming that they will continue to operate, should make the valuation of property, plant and equipment used in their business activity in accordance with Art. 28. That is: “property, plant and equipment (...) at the acquisition price or manufacturing cost, or adjusted value (after revaluation of property, plant and equipment), less depreciation or amortisation charges and impairment losses; (...) construction in progress – at the total cost relating directly to the purchase or manufacturing thereof, less any impairment losses”. If the going concern assumption is not appropriate, then the enterprise should value its assets in accordance with Art. 29, that is: “the undertaking's assets are measured at net realisable selling prices no higher than their acquisition prices or manufacturing costs, less any accumulated depreciation or amortisation charges as well as impairment losses recognised so far. (...) Measurement at net selling prices (...) should take place in particular on the day preceding the day of an undertaking being put into liquidation or declared bankrupt, at the end of a financial year, if on the date of approval of the financial statements for a given financial year the undertaking does not continue

its operations, at the end of a financial year falling in the course of liquidation or bankruptcy proceedings”.

The enterprises which draw up financial statements in accordance with IAS/IFRS have the right to choose the valuation of property, plant and equipment in accordance with IAS 16 at their historical cost or at the reassessed value to the fair value level. If the going concern assumption is not appropriate and the sale of property, plant and equipment is highly probable, the valuation should be made in accordance with IFRS 5 at the lower cost of its carrying amount or its fair value less costs to sell. In such a case, the property, plant and equipment are presented in the balance sheet under the following entry “Non-current assets held for sale”.

In conclusion, the valuation in accordance with the Polish Accounting Act allows to make depreciation and amortization write-offs and write-offs for impairment losses. It does not allow, however, to increase the value of property, plant and equipment presented in the balance sheet if market value exceeds book value. On the other hand, the valuation in accordance with IAS/IFRS, if it is carried out at the reassessed value, allows to disclose, in the financial statements, the property, plant and equipment revalued “upwards”, if this presents a true and fair situation.

From the point of view of the idea of bankruptcy proceedings, what counts is the information about the current value of the debtor's assets realizable in case of forced sale. From this point of view, the valuation that allows to disclose the value of property, plant and equipment revalued “upwards”, if it is consistent with the real value, is more meaningful than the valuation in accordance with the Polish Accounting Act.

7. VALUATION OF PROPERTY, PLANT AND EQUIPMENT IN BANKRUPTCY PROCEEDINGS IN POLAND

The subject of research is focused on the value of property, plant and equipment presented in the financial statements of the company at risk of bankruptcy. The study material was obtained in the district courts in Warsaw, Cracow, Katowice and Tarnów, from the departments involved in bankruptcy proceedings.

Empirical studies carried out on a group of 100 companies which the court declared bankrupt in 2011. The sample survey constitutes 14% of the population and is a significant representation of the phenomenon in Poland (detailed description of the sample was presented in Bauer, 2013, p. 608–609).

It is worth noting that only in one of the above-mentioned cases, the bankruptcy proceedings concerned an enterprise drawing up financial statements in accordance with IFRS.

The study included balance sheets filed with the court together with the petition to declare bankruptcy. The study is the continuation of previous research carried out by the author.

As a result of the initial phases of the study it was found that (Bauer, 2013, p. 609–615):

- the bankruptcy proceedings documentation collected in the courts provides, in most cases, the information about the book value and the estimated value of property, plant and equipment,
- in 75 cases, the debtor had not filed the balance sheet with the court, which is consistent with the Act on Bankruptcy and Rehabilitation, but denies information on the book value of property, plant and equipment. In 26% of cases, the interim court supervisor had not been appointed, which made it impossible to compare the book value and the estimated value of property, plant and equipment;
- limiting the legal requirements of the debtors facing bankruptcy to submit the balance sheet deprives its users of information about whether the balance sheet valuation had been prepared according to the going concern assumption;
- the estimated value of property, plant and equipment made by debtors and interim court supervisors differ from the carrying amounts. Simple linear regression analysis has been

used to describe the dependence. The model of dependence based on the estimated valuation of assets made by the debtor, drawn up on the basis of the study sample, indicates that this valuation is nearly 35% higher than the carrying amount. This model is characterized by very high coefficient of determination value, equal to 88.1%, which indicates that the value of property, plant and equipment valued by the debtors are highly dependent on the carrying amount. Extending the results obtained for the given sample to the whole population, it can be concluded with 95% probability that the regression coefficient is estimated in the 1.221 to 1.468 range. However, the property, plant and equipment pricing model made by the interim court supervisor displays an inverse relationship. The estimated value of property, plant and equipment represents on average approximately 75% of the carrying amount. The model itself is not so precise – only 76% of dependencies can be explained using it.

- There are also large differences between the estimated valuation made by debtors and interim court supervisors. The study shows that the image presented in the estimated valuation made by the debtor is more advantageous. Debtors make upward revaluations more often than interim court supervisors. The reason for this is manifest while analysing in detail the financial statements submitted to the court by interim court supervisors who relate to the valuation made by the debtors, stressing that the sale value will be lower in case of enforced sale. While studying the relationship between the valuations made by interim court supervisors and debtors, the best match to the study results has been obtained for the linear regression model without intercept. The model is characterized by the coefficient of determination reaching nearly 86%, it can be concluded that this model describes accurately the studied relationship. The resulting confidence interval for the regression coefficient is relatively narrow, which means that it can be concluded with very high probability (95%) that within the entire statistical population of enterprises undergoing bankruptcy proceedings, the value of property, plant and equipment determined by interim court supervisors will represent on average 50-61% of the value presented by debtors;
- what counts for the court is the realizable, commercial or use value of property, plant and equipment that will be used to settle creditors' claims.

For further study, 50 cases have been selected, in which the bankruptcy proceeding documentation contained complete information about the carrying and estimated values of the property, plant and equipment and the entire property.

Average share of property, plant and equipment estimated value (EVPPE) in property estimated value (EVP) and share of property, plant and equipment (PPE) in total assets (TA) in the complete sample is 19.9 [%]. However the value of standard deviation amounts 24.4 [%], it results with coefficient of variation on the level 122 [%]. The confidence interval for average share of EVPPE in EVP and share of PPE in TA (based on 95% confidence level) is reasonably wide – it is [14.8; 25.1] [%]. These results indicate significant variation of obtained results.

The best fitting for the relationship between share of EVPPE in EVP and share of PPE in TA was achieved in case of a double square root model:

$$\text{EVPPE /EVP} = (0,137 + 0,616221*\text{sqrt}(\text{PPE/TA} [-]))^2$$

The fitted model on the background of the sample is presented on the Figure 1.

The parameters of the model are statistically significant on the 95% confidence level. The R-Squared statistic indicates that the model as fitted explains 37% of the variability in share of EVPPE in EVP after transforming to a logarithmic scale to linearize the model. The correlation coefficient equals 0.61, indicating medium relationship between the variables.

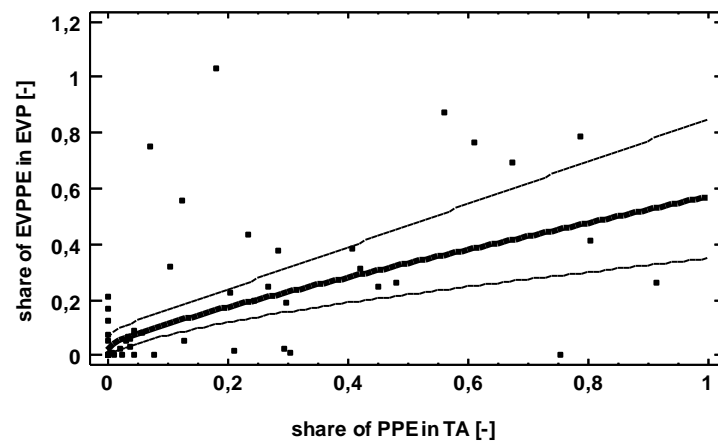


Fig. 1. Simple regression model to describe the relationship between share of property, plant and equipment estimated value (EVPPE) in property estimated value (EVP) and share of property, plant and equipment (PPE) in total assets (TA)

6. CONCLUSIONS

Globalisation of the world's economy, intensification of competition, technological development and a widespread application of information technology influence changes in the business environment and insolvency and accounting law as well.

Individual judgement of entity financial situation is inevitable in the complex environment in which companies function. However, proper use of well-prepared financial statements are of fundamental importance for economies. For investors, quality financial statements allows to make them rational investment decisions. On the other hand, the financial statement is helpfull in supporting the court decision-making process in insolvency proceedings of companies at bankruptcy risk.

The timing and the threat of bankruptcy could have a significant impact on the value of the property. The inability to revalue the assets "upwards" to market value in the case of the balance sheet valuation of assets on the basis of historical cost and the inability to properly assess the market and estimated values of assets may result in the entity's financial standing presented in the financial statements differing from reality. In the initial bankruptcy proceedings, it is not known how the market will value the assets of a given company, for the sale of the assets, its separate parts or the entire enterprise takes place only after the bankruptcy has been declared.

The results of this study indicate that the carrying value of property, plant and equipment in the financial statements of the company at bankruptcy risk differs from the estimated valuation. The results show the differences between the values of property, plant and equipment (i.e. the carrying and estimated values) and their shares in the carrying and estimated values of the property.

One question remains problematic in this context, namely whether the financial statements of the entity at risk of bankruptcy have any relevance in bankruptcy proceedings. The bankruptcy proceedings documentation contains visible references to the carrying amounts as a starting point to estimate the valuation of assets. However, only in a few cases (9.6%), the carrying value of property, plant and equipment was recognized by the interim court supervisor as equal to the estimated value.

The results of the study indicate the need for further analysis of the valuation of assets of companies facing bankruptcy, as well as in the later stages of bankruptcy proceedings.

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RE-ESTABLISHING TRUST AND ETHICAL LEADERSHIP

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Abstract: *The breakdown of public trust in the profession is a very significant and damaging trend, and something expected to get worse if we don't address it.*

We are genuinely recording a significant breakdown of public trust – in both accountancy, and in business, and even what it means to be a 'professional'.

It is vital that the profession learns to better communicate its value – and we at ACCA must play an active role in doing so. Failure to do so will fundamentally affect the future development of the profession, and its place in the global workplace.

We must respond to these pressures by working to strengthen our public image and go beyond current financial reporting practices to provide a more transparent, simplified but holistic picture of a firm's health and prospects. Professional Accountants must be seen as part of the solution, nor part of the problem and therefore, it is essential that Accountants must re-establish trust and ethical leadership.

Accountants should play a public guardianship role – to be working in the public interest is a key tenet of what it means to be a professional. Some of that has been lost, and some of it misunderstood by the public. The future success of the profession at large depends on us regaining the public's trust.

Keywords: *Ethics, Leadership, Professional, Trust*

ASSESSING ACCOUNTING STUDENTS' ACADEMIC PERFORMANCE: A CASE STUDY ON ROMANIA

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Abstract: *We propose a research design involving the use of Bloom's taxonomy both in facilitating the teaching-learning process and in the educator assessing students' final grades. The latter are compared with students' self-acknowledged grades. Testing is done by considering a sample of accounting students enrolled for the Controlling course in Romania. The employed research methodology relies on two instruments: a questionnaire and the examination process. Cluster analysis is used in analyzing students' grades. Determinants of students' academic performance are discussed by using factor analysis. Comparing students' self-acknowledged grades with those assessed by the educator, we document the necessity of further work in enhancing students' ability to better assess their academic performance. Questions belonging to the application and analysis levels seem to be preferred by students. We raise a series of theoretical questions in the area of examination performance. The obtained results in relation to the assessment of accounting students' academic performance and its determinants offer useful insights for accounting educators. Our paper tests the use of Bloom's taxonomy in the context of an emerging country's educational system that lacked consistency and faced significant challenges throughout history. We also consider two measures for students' academic performance as perceptions upon what should be the same result of the teaching learning process. The paper addresses the evolutions and particularities of the Romanian academic environment in the area of economics, developing a brief analysis meant to position the testing of the proposed research design.*

Keywords: *accounting students, examination performance, Bloom's taxonomy, self-acknowledgement*

CULTURE AND ORGANIZATIONS: THEORETICAL FRAMEWORKS AND RELEVANT FINDINGS RELATED TO INTERCULTURAL COMMUNICATION COMPETENCE AND ACCOUNTING PRACTICES

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Abstract: *Social science research shows that cultural values are developed throughout one's life and shaped by various factors, including informal and formal socialization and schooling practices that in turn influence the development of social capital (Veselý, 2006). Cultural differences have become the object of study within a growing interdisciplinary field, including cultural psychologists and anthropologists (Machová and Kubátová, 1995; Hofstede, 2002).*

*(1) The first framework draws upon the work of **Geert Hofstede**, an organizational psychologist whose research was based on a large, questionnaire survey of IBM employees and managers in forty different countries (Hofstede, 2001).*

*(2) The second framework utilizes research by **Fons Trompenaars and Charles Hampden-Turner** (1993) who identified several elementary dimensions according to which different cultures can be measured (Trompenaars, Hampden-Turner, 2001).*

*(3) The third framework draws upon **Milton Bennett's** Developmental Model of Intercultural Sensitivity (1993) which explains the reaction to cultural differences through one's experience of cultural difference.*

*(4) The fourth powerful framework relevant for studies of cultural values and multicultural environment has been elaborated by **Edward Hall**.*

Keywords: *Bennett, cultural differences, Hall, Hofstede, Trompenaars*

INTRODUCTION

Within increasingly interdependent economies and societies, accounting practices are highly correlated with intercultural competence; intercultural competence is a developmental process with traits and dimensions that demonstrate the ability to effectively deal with cultural differences in order to develop successful cooperation with others. It involves a complex set of abilities needed to perform appropriately when interacting with others who are linguistically and culturally different from oneself.

A recent national survey of the Organization for Economic Cooperation and Development (OECD) to which the EU Commission and Czech Republic are members, recommended that Czech Republic increase its labor market flexibility by strengthening its education system. Employers' reports, statistics on secondary school graduates' employment rate and recent research studies, support the OECD's recommendation with the finding that domestic and international companies operating in Czech Republic are currently demanding certain intercultural communication competences (ICC) from their employees. Fresh Minds Limited survey of 500 European business leaders identified the skills young people should possess and revealed a lack of 'soft skills' such as confidence, teamwork, self-motivation and presentation. Two-thirds of the respondents believe that their countries' education systems do not successfully instill these skills. A similar study by surveyed over 2,000 companies in the Moravian-Silesian region and identified 14 competencies of skills, attitudes, knowledge and behaviors necessary for success at work, highlighting teamwork and communication. The report concluded ICC have

been implemented with limited success in Czech Republic schools and cited social capital as deficient in this area.

Social capital is theorized as a result of how people interact and benefit from their mutual relationships within social networks (Dekker and Uslaner, 2001, pg. 73). As social capital is becoming increasingly necessary to the current and future workplace, our article will contribute to an understanding of the relationship of ICC to the development of cognitive social capital relevant for accounting, to which the OECD is directing Czech Republic's transition to a more innovative, skill-based economy.

Intercultural competence (IC) is understood as involving multiple modes of communication, (i.e., verbal, non-verbal, gestural, representational, etc.) through which individuals who inhabit certain cultures live their values. As assessing intercultural competence is best conducted through a mixed method approach to quantitative and qualitative measures (Deardorff, 2006, pg. 255), there have been selected interdisciplinary frameworks in order to measure ICC's strengths and weaknesses in organizations.

The aim of the paper is to elucidate four theoretical frameworks and to present current issues concerning development of intercultural communication competence relevant for accounting practices.

1. IMPORTANCE OF HOFSTEDE'S DIMENSIONS OF HIGH&LOW POWER DISTANCE AND HIGH&LOW UNCERTAINTY AVOIDANCE FOR DEVELOPMENT OF ICC

The first framework draws upon the work of **Geert Hofstede**, an organizational psychologist whose research was based on a large, questionnaire survey of IBM employees and managers in forty different countries (Hofstede, 2001, pg. 326). Hofstede identifies cultural values along the dimensions of power distance, uncertainty avoidance, individualism and masculinity.

Example: High Power Distance & Low Power Distance

A) These behaviours are more commonly associated with high power distance cultures.

1. People are less likely to question the boss. (There is more fear of displeasing the boss in high power distance cultures). 2. Elitism is the norm (Emphasizing distinctions between boss and subordinates is the norm). 3. Those of power have special privileges (Rank has its privileges in these cultures). 4. There are greater wage differences between managers and subordinates (Again, to emphasize the distance). 5. Workers prefer precise instructions from superiors. (Close supervision, the visible exercise of power, is common to these cultures). 6. Bosses are independent, subordinates are dependent. (The unequal distribution of power). 7. Freedom of thought could get you into trouble. (Independence is not valued in subordinates). 8. Less social mobility is the norm. (To keep those with and without power separated). 9. The chain of command is sacred. (Rank must be respected; you should not go around people). 10. The pecking order is clearly established. (There is a need to determine who has power over whom). 11. Management style is authoritarian and paternalistic (Bosses are supposed to wield their power). 12. Interaction between boss and subordinate is formal (To emphasize the power gap).

B) These behaviours are more commonly associated with low power distance forces.

1. Students question teachers (Because superiors do not have to be deferred to). 2. Freedom of thought is encouraged (No one is threatened by independence of thinking for oneself). 3. The chain of command is mainly for convenience (Power differences are not emphasized). 4. Interaction between boss and subordinate is more informal. (Because the distance is minimized). 5. Subordinates and bosses are independent. (We are all equal here so we all depend on each other). 6. It's okay to question the boss. (Because he's just another worker here). 7. Management style is consultative and democratic (Because we are all in this together, power distance is de-emphasized).

Belgium					X		
Czech Republic					X		
Denmark		X					
Finland		X					
Italy		X					
Netherlands		X					
Portugal					X		
Greece				X			
United Kingdom		X					
10	20	30	40	50	60	70	80

Fig. 1. Power distance index in selected countries of European Union. Source: Světlík, J. (2003): *Marketing pro světový trh [Marketing for World Market]*, Grada, 1st Edition, pg. 46.

Example: Individualism&Collectivism

1. Managers should be hired from within the organization, based mainly on their seniority (**Collectivism**). Managers should be hired on the basis of the skills they have and previous experience in similar jobs (**Individualism**).
2. It takes a long time to make a new friend (**Collectivism**). Friends can be made relatively quickly (**Individualism**).
3. If I took a job with a new company, I would expect my old employer to wish me well (**Individualism**). If I took a job with a new company, I would be afraid that my employer might lose face (**Collectivism**).
4. I expect people to judge me by my achievements (**Individualism**). I expect people to judge me by my affiliations (**Collectivism**).
5. Before making a decision, it is best to make sure everyone agrees with it (**Collectivism**). Before making a decision, you should get at least half of the people to agree with it (**Individualism**).
6. I am embarassed by individual recognition (**Collectivism**). If I do a good job, I feel I have earned individual recognition (**Individualism**).
7. Making sure people don't lose face is more important than always being completely honest (**Collectivism**). Being straight with people is always best in the end (**Individualism**).
8. If my brother or sister did wrong, I would admit this to other people (**Individualism**). If my brother or sister did wrong, I would defend them to other people (**Collectivism**).
9. Confrontation is sometimes necessary to clear the air (**Individualism**). Confrontation almost always cause more problems than it solves (**Collectivism**).
10. In the end, you can always rely on other people (**Collectivism**). In the end, you can only rely on yourself (**Individualism**).

Belgium						X	
Czech Republic				X			
Denmark						X	
Finland					X		
Italy						X	
Netherlands							X
Portugal	X						
Greece		X					
United Kingdom							X
10	20	30	40	50	60	70	80

Fig. 2. Individualism index in selected countries of European Union. Source: Světlík, J. (2003): *Marketing pro světový trh [Marketing for World Market]*, Grada, 1st Edition, Praha, pg. 52.

Along the power distance dimension, the Czech society exhibits high power distance, similarly as French and Belgian societies (Světlik, 2003, pg. 46). People tend to accept and expect a hierarchical/unequal distribution of power. According to the uncertainty avoidance dimension, the Czech society (similarly as German) tends to avoid risk. This dimension measures the degree to which members of a given society deal with uncertainty and risk of everyday life, and prefer working with long-term acquaintances and friends rather than strangers. The individualism dimension measures the degree to which individuals perceive themselves as separate from others or free from group pressure to conform. Individualism in the Czech society comes out in the middle (Světlik, 2003, pg. 52). Despite the fact that Hofstede ignores intergenerational differences and distinctions among members of the same nation or ethnic group, his dimensions are particularly useful for understanding conflicts among various groups from different cultural backgrounds that could be important for accounting practices.

Belgium				X			
Czech Republic	X						
Denmark	X						
Finland	X						
Italy						X	
Netherlands	X						
Portugal			X				
Greece				X			
United Kingdom					X		
10	20	30	40	50	60	70	80

Fig. 3. Masculinity index in selected countries of European Union. Source: Světlik, J. (2003): *Marketing pro světový trh [Marketing for World Market]*, Grada, 1st Edition, Praha, pg. 56.

2. IMPORTANCE OF FONS TROMPENAARS' DIMENSIONS OF PARTICULARISM & UNIVERSALISM AND ASCRIPTION & ACHIEVEMENT FOR DEVELOPMENT OF ICC

The second framework utilizes research by **Fons Trompenaars and Charles Hampden-Turner** (1993) who identified several elementary dimensions according to which different cultures can be measured (Trompenaars, Humpden-Turner, 1997, pg. 10–302). According to the first one (universalism vs particularism) Czech society is more similar to Mediterranean societies, which are more particularistic. Universalistic societies place more emphasis on, and expect others to follow, given rules, while particularistic ones stress personal and contextual aspects in interpreting rules.

Example: Universalism & Particularism

- 1.a. In society, we should help those who are the neediest (**Universalism**). 1.b. In society, we should help the neediest of those who depend on us (**Particularism**).
- 2.a. There are no absolutes in life, you always have to look at the particular situation (**Particularism**). 2.b. There are certain absolutes which apply across the board (**Universalism**).
- 3.a. The courts should mediate conflicts (**Universalism**). 3.b. People should solve their own conflicts; it's embarrassing if it has to go to court (**Particularism**).
- 4.a. In general, people can be trusted (**Universalism**). 4.b. My closest associates can be trusted absolutely; everyone else is automatically suspect (**Particularism**).

- 5.a. *In hiring someone, I want to know about their technical skills and their educational/professional background (Universalism).* 5.b. *In hiring, I want to know who the person's family and friends are, who will vouch for this person (Particularism).*
- 6.a. *I would be very hurt if my neighbour, a policeman, gave me a ticket for speeding (Particularism).* 6.b. *I would not expect my neighbour, the policeman, to jeopardize his job and not give me a speeding ticket (Universalism).*
- 7.a. *Performance reviews should not take personal relations into account (Universalism).* 7.b. *Performance review inevitably take personal relations into account (Particularism).*
- 8.a. *You often have to make exceptions for people because of circumstances (Universalism).* 8.b. *Exceptions should be very rare; otherwise, you open the floodgates (Particularism).*
- 9.a. *Contracts aren't necessary between friends (Particularism).* 9.b. *Contracts guarantee that friends stay friends (Universalism).*
- 10.a. *What is ethical in a given situation depends on who you are dealing with (Particularism).*

According to the second dimension (display of emotions in communication), Czechs are also in the middle compared to inhabitants of Mediterranean cultures, who speak quickly, raise their voice and show their enthusiasm or sadness, while in Scandinavian countries expression of emotions is considered to be a professional deficiency or uneasiness. According to the third dimension (specificity) Czech culture is more diffuse than specific. This dimension measures whether life is considered to be composed of many components which are not interchangeable and therefore deems it is necessary to divide work and private matters and activities or whether there is an assumption that all elements are part of the whole and mutually related.

According to the fourth dimension success, Czech can also be placed in the middle of the scale. This dimension measures whether an individual has achieved success on the basis of his or her efforts or work (North American culture) or whether status is more ascribed by means of a combination of personality of the individual as well as his or her social origins, education, employment and membership of this or that group.

3. IMPORTANCE OF MILTON BENNETT'S ATTITUDES TOWARD CULTURAL DIFFERENCE FOR DEVELOPMENT OF ICC

The third framework draws upon **Milton Bennett's** Developmental Model of Intercultural Sensitivity (2001) which explains the reaction to cultural differences through one's experience of cultural difference. As one's experience becomes more complex, one develops a greater potential for competence in ICC interactions. This model is activated by cognitive structures (i.e. worldviews) that range from ethnocentric to ethno-relative. Those who approach ethno-relative worldviews are more likely to exhibit cultural competence.

The ethnocentric continuum ranges from Defense/Denial, Reversal and Minimization to the ethno-relative stages of Acceptance, Adaptation (including cognitive frame-shifting and behavioural code-switching) and Encapsulated Marginality. According to the principle Denial of Difference individuals experience their own culture as the only "real" one. Other cultures are either not noticed at all or they are understood in an undifferentiated, simplistic manner. People at this position are not interested in cultural difference, but when confronted with it, their rejection of acceptance may change to aggressive attempts to avoid or eliminate it.

According to the Principle Defence against Difference one's culture is experienced as the most "evolved" or best way to live. This position is characterized by dualistic thinking and frequently accompanied by overtly negative stereotyping. Actors in this position are more openly threatened by cultural difference and more likely to be acting aggressively against it.

According to the principle Minimization of Difference the experience of similarity outweighs the experience of difference. Actors recognize superficial cultural differences in food, customs, etc., but they emphasize human similarity in psychological structure, psychological needs, and/or assumed adherence to universal values. Hammer (1999) has applied this theory to developing Intercultural Development Inventory instrument to measure one's orientation towards cultural differences that can be used to enhance students' ICC competence. Bennett's framework is very suitable for development of ICC since it has provided tools how to reach the phase in which difference is seen as normal and integrated into the identity of oneself; at the final phase one can relate to several cultural reference frameworks.

I. Initial Enthusiasm (The Honeymoon): First week or two in host country

Characteristics. Exposure to country and culture is limited. Excitement and enthusiasm abound. Everything is exotic and quaint. Attitude toward host country is generally limited. Little is expected of you.

II. Initial Country&Culture Shock: First few weeks; first half of training

Characteristics. Wider exposure to country and culture means more realistic and more mixed reactions. Enthusiasm is tempered with frustration. Feelings of vulnerability and dependence are common. Homesickness is frequent. Nothing is routine. Limited language ability undermines confidence. Close bonds are formed with other trainees.

III. Initial Adjustment: Second half of training

Characteristics: Second half of training. Routines are reestablished. Some aspects of the country and culture are now seen as normal. Adjustment to the physical aspects of the host country is better. You are somewhat more self-reliant. You are more positive about your ability to function in country. Adjustment is to the culture of pre-service training as much as it is to host country culture.

IV. Further Culture Shock: First few months after training; settling-in period

Your experience post-training withdrawal symptoms. You're adjusting to being on your own country. It's your first experience taking care of yourself in country. You're having your first encounters with the workrelated aspects of culture, with initial surprises and frustrations. You miss daily contact with your community of the country of your origin and your version of the local language. You're surprised at still having culture shock to go through (you thought you adjusted during pre-service training).

V. Further Adjustment: Post settling-in

You are getting used to being on your own. You're better able to take care of yourself. You're making friends in the community. You speak the language better. You're more effective at work because you understand the culture better.

4. IMPORTANCE OF EDWARD HALL'S CONCEPT OF HIGH CONTEXT&LOW CONTEXT COMMUNICATION AND MONOCHRONIC&POLYCHRONIC UNDERSTANDING OF TIME FOR DEVELOPMENT OF ICC

The fourth powerful framework relevant for studies of cultural values and multicultural environment has been elaborated by **Edward Hall**, who has spent more than forty years developing and writing about a four-dimensional classification system which basically focuses on the communication patterns found within various cultural environments and emphasizes four dimensions along which societies can be compared (Hall, 1962, pg. 78–153).

The first dimension (high and low context) measures communication context or the amount of information that must be explicitly stated if a message or communication is to be successful. The Czech society has been placed around average; for example, the Japanese have been determined to use high context communication on the one hand, and the Americans low context communication on the other one

Examples of Directness

I don't think that's such a good idea. That's not the point. I think we should...What do you think, Mr. Cato? Those figures are not accurate. You're doing that wrong. I don't agree.

Examples of Indirectness

That is very interesting point. This proposal deserves further consideration. I know very little about this, but...We understand your proposal very well. We will try our best. I heard another story about that project. Can we move on to the next topic?

According to the second dimension (ways of communicating through specific handling of personal space), the Czechs are also placed in the middle along this scale, between Scandinavians on one extreme, who tend to keep more place between them than do Mediterranean cultures, at the other extreme.

According to the third dimension (concept of time), Czechs also tend to be in the middle between German monochronic understanding of time (preference for scheduling and completing one activity at a time) and Mediterranean polychronic conception (not distinguishing between activities and completing them simultaneously)

According to the fourth dimension (speed and structure of messages between individuals or organizations), the Czech society has been placed between North American and South American styles. In North American, speed and structure of messages between individuals or organizations has been noted as significantly higher than in South America or in developing countries.

Example: Monochronic&Polychronic

- 1.a. People should stand in line so they can be waited on one at a time (**Monochronic**).*
- 1.b. There's no need to stand in line, as people will be waited on as they are ready for service (**Polychronic**).*
- 2.a. Interruptions usually cannot be avoided and are often quite beneficial (**Polychronic**).*
- 2.b. Interruptions should be avoided wherever possible (**Monochronic**).*
- 3.a. It's more efficient if you do one thing at a time (**Monochronic**).*
- 3.b. I can get as much done if I work on two or three things at the same time (**Polychronic**).*
- 4.a. It's more important to complete the transaction (**Polychronic**).*
- 4.b. It's more important to stick to the schedule (**Monochronic**).*
- 5.a. Unanticipated events are hard to accommodate and should be avoided where possible (**Monochronic**).*
- 5.b. Unexpected things happen all the time, that's life (**Polychronic**).*
- 6.a. You shouldn't take a telephone call or acknowledge a visitor when you are meeting with another person (**Monochronic**).*
- 6.b. I would be rude not to take a phone call if I'm in, or to ignore a visitor who drops by (**Polychronic**).*
- 7.a. You shouldn't take deadlines too seriously; anything can happen. What's a deadline between friends? (**Polychronic**).*
- 7.b. Deadlines are like a promise; many other things depend on them, so they should not be treated lightly (**Monochronic**).*
- 8.a. It's important, in a meeting or a conversation, not to become distracted or digress. You should stick to the agenda (**Monochronic**).*
- 8.b. Digressions, distractions are inevitable. An agenda is just a piece of paper (**Polychronic**).*

- 9.a. *I tend to be people-oriented (Polychronic).* 9.b. *I tend to be task-oriented (Monochronic).*
 10.a. *Personal talk is part of the job (Polychronic).* 10.b. *Personal talk should be saved for after hours or during lunch (Monochronic).*

CURRENT ISSUES RELATED TO ADVANCEMENT OF ICC IN THE CZECH REPUBLIC

Intercultural Competence in the Czech Republic Has Been Recently Evaluated as Inadequate

In the Czech Republic ICC has been recently evaluated as inadequate due to deficiencies related to labour market structures as well as other variables. Cultural values, coupled with cultural awareness, are known to have a primary role in the development of tolerance and acceptance of cultural differences, reduction of cultural bias and minimization of related social conflicts (LeBaron, 2001, pg. 1–20). While national cultures have been identified across Europe according to their value dimensions and differences (Trompenaars and Hampden-Turner, 1993, pg. 230–272), the development of intercultural competence in relationship to local cultural values as transmitted through schools has not been studied.

The essentialist position situates culture as immutable (Peterson, 2004, pg. 102–163). However, difficulties in transmitting EU cultural values appear to stem from the lack of a common culture upon which to build an EU identity. Research reveals nation-state identities being rooted more firmly than an European Union identity. Reports based on this research overlook the impact national cultural values have upon cultural identities, where perceptions of ‘self’ and ‘others’ may interfere with interpersonal communications.

Considering culture as learned, reciprocal, and collective, the article acknowledges that multiple factors affect the formation of students’ cultural values, including family, speech communities, social media, subcultures, gaming, and Internet use. International research has demonstrated that students’ exposure to other cultures can increase intercultural sensitivity and adaptability, and may increase their ICC (Bennett, 2001, pg. 10–30).

Theories in the ICC field have been criticized for being biased towards the individualistic, the western way of managing communication and its conflicts (Oetzel and Ting-Toomey, 2013, pg. 231–258); thus, Czech companies and society needs to be studied within its local cultural values and their variables.

Communication competence and intercultural competence have been established fields of study for at least fifty years and draw upon diverse perspectives from interdisciplinary fields. Whereas the term ICC is increasingly used in the cross-cultural communication field, it represents only one term among many that are used to address what transpires during intercultural encounters.

Although articulated theoretically, ICC research lacks specific data across cultural and situational contexts (Witteborn, 2007, pg. 556–575). ICC may be measured through domains, dimensions, proficiencies, and developmental levels affecting relationships, communication, and collaboration. Lacking consensus of ICC’s unifying features and with a diversity of instruments to measure it, ICC is continually evolving.

Areas that need more study include the study of language, the role of intergroup perceptions to communication between ethnic and cultural groups, how cultural perspectives and misunderstanding contribute to intercultural conflicts in the local context, and the impact of ICC training and skills development with teachers.

According to Ingrid Piller language is primarily the channel of socialization that binds speakers into communities but its meaning and nuances transpire through a process of negotiation connected to cultural backgrounds. Speakers are naturally and unconsciously positioned to assume attitudes towards someone’s language, character and cultural values based

on dialect or ability to speak a language (Piller, 2011, pg. 11–57). Piller emphasizes the importance of language proficiency for ICC and highlights its hindrances such as people's unwillingness to negotiate and get along, prejudice about accents, ignorance of local values and of options in performing speech acts and rituals.

Oetzel' and Ting-Toomey's research (2006) supports the need for awareness of how to act appropriately with members of another language-culture on their terms. Speakers of multiple languages have options of language rituals, conversation strategies, visual means of communication, body language, space, and other means at their disposal when communicating with members of other cultures.

CONCLUSION

Given above mentioned frameworks and findings, further research concerning cultural differences that could be relevant for accounting practices should focus on the following issues.

- 1) Behaviour of accountants and accounts managers in various countries of European Union as well as elsewhere differ in their acceptance of power or superior-subordinate relationships. In what specific ways do educational institutions and companies prepare accountants and accounts managers to accept various types of communication structures?
- 2) Power relationships are played out in language. Are those relationships sensitive to patterns, rituals, speech acts and language ideologies present in the companies?
- 3) Rituals of politeness (such as in greeting, complementing, requesting, inquiring, etc.) are negotiated within the cultural values of the company. Does the majority language alone establish the protocols? What role does the company management assume in the negotiation?
- 4) Language ideology (having a status of a national, official, vernacular, standard or local language) affects one's willingness to engage in ICC. In what specific ways are speakers' attitudes reflected in ICC relevant for accounting practices?
- 5) Language proficiency affects ICC and modes of cooperation including accountants's practices. What is the participants' proficiency in the companies' majority and minority language(s)?
- 6) Risk avoidance is related to unequal representation in the companies. Do differences between cultural identities of accountants and accounts managers in companies influence overall risk avoidance level displayed in the company?
- 7) What are the discrepancies between stated belief and practice (despite managers and accountants claiming to be open-minded and tolerant)? Are the factors of language prestige, ideology and proficiency underestimated in their effect on one's status and self-perception? To what degree is management aware of the issues of risk avoidance and how do they guarantee account managers' and accountants' right of democratic representation?
- 8) In what specific ways does the company environment encourage the development of ICC competence (by means of regular and systematic training) and interaction with diverse groups, and promote tolerant understanding of cultural differences? Do companies reflect diversity in the use of space, choice between individualist or collective learning styles, and verbal or non-verbal communication strategies?
- 9) What is the level of intercultural sensitivity and awareness of the participants in the company environment? How does the level of cultural sensitivity and awareness impact interpersonal interactions, working environments, company policies and practices?
- 10) In what ways do company environments differ in enforcing rules and handling individual preferences? What differences exist between accounts managers and accountants who work in Czech and international companies?
- 11) What differences exist in accountants' orientation towards the individual and the group? Are accountants from individualist cultures positive about learning new topics and speaking up at the workplace? Do those from collectivist cultures tend to speak up only when called on and avoid challenging the superior (particularly accounts manager)?

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ASSESSMENT OF SMALL AND MEDIUM ENTERPRISES' USING MARKETING ANALYTICS IN MEXICO

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Abstract: *This paper aims to focus on the determinants influencing the internationalization of small and medium-sized enterprises (SMEs) in Mexico. The objective is to investigate and evaluate the business environment and, then, examine the importance of developing and promoting entrepreneurship to allow SMEs in Mexico to develop a competitive position in the international marketplace. An overview is provided of the current economic situation facing SMEs in Mexico. Then factors necessary for the expansion of the business will be discussed, along with the challenges of overcoming the resource gaps to be identified. We have conducted empirical surveys along with the use of SPSS statistical tools to predict the potential of revenue growth in SME sector. Information is provided concerning the current situation for SMEs in Mexico and the challenges encountered as they face a business environment that is becoming more competitive. We also found that SMEs are increasingly more integrated to global economy and not limited to regional/international activities. Quantitative analysis shows that there is significant potential for SME for next couple of year despite economic uncertainty. This paper integrates entrepreneurship, and the resource-based internationalization of SMEs in Mexico, specifically focusing on the use of technology.*

Keywords: *Entrepreneurs, International trade, Small & medium-sized enterprises, Marketing Analytics*

JEL Classification: C40, C49, C63, C81, C83

1. INTRODUCTION

In an exacting economic environment, small and medium sized enterprises (SMEs) have been presented with a challenge; to progressively increase the profitability of their businesses against a backdrop of commonly weak demand. This report summarizes the results of research into the performance and competitiveness of SMEs in this business environment, with a specific focus on attempts by SMEs to ‘internationalize’ their businesses and how this impacts on their growth.

1.1 The definition of SMEs

Small and medium-sized enterprises (SMEs) are a very heterogeneous group. SMEs are found in a wide array of business activities, ranging from the single artisan producing agricultural implements for the village market, the coffee shop at the corner, the internet cafe in a small town to a small sophisticated engineering or software firm selling to overseas markets, and a medium-sized automotive parts manufacturer selling to multinational automakers in the domestic and foreign markets. The owners may or may not be poor; while the firms operate in very different markets (urban, rural, local, national, regional and international) which embodies different levels of skills, capital, sophistication and growth orientation, and may be in the formal or the informal economy.

Statistical definition of SMEs varies by country but is usually based on the number of employees, value of sales and/or value of assets. Due to its ease of collection, the most commonly used variable is the number of employees. The EU, a large number of OECD members, transition

and developing countries set the upper limit of number of employees in the SMEs between 200-250, with a few exceptions such as Japan (300 employees) and the USA (500 employees).

At the lower end of the SME sector, a large number of countries define a group, making up a mixture of the self-employed and “micro” enterprises, with less than 10 employees. Irrespective of the level of development of an economy, a significant proportion of micro and, sometimes, small enterprises are found in the informal sector, or the shadow economy. Schneider (2003) compared the size of the informal sector in 22 transition (former Soviet Union and Central and Eastern Europe) and 21 OECD economies from 2000-2002 and found that the size of the informal sector amounted to an average of 16.7%, 29.2% and 44.8% of GDP in OECD, Central and Eastern Europe and the former Soviet Union economies, respectively.

1.2 The importance of SMEs in a global economy

Global economic integration is changing the competitive paradigm in which all businesses operate, requiring an international expansion strategy to positively impact long-term growth and survival (Karagozoglu and Lindell, 1998). The small business sector has become more important as they emerge as a dominant force impacting the growth of national economies (Shridhar, 2006). Although, there are a number of disadvantages inherently faced by SMEs as they transition into international environments (Chen and Huang, 2004). Managers of non-exporting SMEs perceive the international environment as being risky, unprofitable and unmanageable, primarily due to misinformation and lack of experience with global business (Malekzadeh and Nahavandi, 1985). SMEs, due to their size limitations, often have limited financial capital and a lack of necessary human resources. Many operators of small businesses lack experience in developing an international strategy (Tesar and Moini, 1998). There are also disadvantages related to a lack of competitive power as a consequence of the size of the organization. SMEs have difficulty in influencing global pricing as they rely on only a small customer base, and are limited in expansion due to minimal access to financial resources (Kalantaridis, 2004). Faced with the need to overcome significant weaknesses, the strategic importance of SMEs has been identified in several factors. They are responsible for growing employment at a faster rate than organizations; they increase the competitive intensity of the market and reduce the monopolistic positions of large organizations; they encourage the development of entrepreneurial skills and innovation. Larger SMEs in the USA, account for three out of every four new jobs and contribute to providing over half of the gross domestic product (Underwood, 2004). From 1992 to 1999, the number of SMEs that were involved in exporting increased over 100 percent, to nearly 97 percent of all exporting firms in the USA, and accounting for \$168.5 billion in value (Underwood, 2004).

SMEs typically provide capabilities that their larger customers do not have nor cannot cost-effectively create such as:

- Agility in responding to changes in technologies, markets, and trends,
- Efficiency due, in part, to less bureaucracy,
- Initiative and entrepreneurial behavior on the part of employees resulting in higher levels of creativity and energy and a greater desire for success,
- Access to specialized proprietary technologies, process capabilities, and expertise,
- Shorter time-to-market because operations are small and focused,
- Lower labor costs and less restrictive labor contracts,
- Spreading the costs of specialized capabilities over larger production volumes by serving multiple customers,
- Lower cost, customer focused, and customized services, including documentation, after-sales support, spare parts, recycling, and disposal.

1.3 SMEs' international competitiveness

As trade barriers are removed, logistics and communication costs fall, small and medium-sized enterprises have adapted to new challenges to stay competitive in an international marketplace. These developments have also opened up opportunities for SMEs. Their integration into the global economy has prompted them to develop new international activities such as attempting to open new markets; adding more value to their products and services; while reducing their cost base. Assessing an SME's international competitiveness requires consideration of the economic, political and social aspects within the SME's country of origin, as much as looking at the SME itself. Both levels of analysis have to be taken into account in this research: The macro level, 'national' competitive advantages, such as access to new technologies, skilled labour, market structure, logistics and infrastructure. The micro level, company-specific competitive advantages, such as price, quality, service, responsiveness and innovation

2. TIME SERIES MODEL OVERVIEW

A time series is a set of observations obtained by measuring a single variable regularly over a period of time. In a series of inventory data, for example, the observations might represent daily inventory levels for several months. A series showing the market share of a product might consist of weekly market share taken over a few years. A series of total sales figures might consist of one observation per month for many years. What each of these examples has in common is that a variable was observed at regular, at known intervals over a certain length of time. Thus, the form of the data for a typical time series is a single sequence or list of observations representing measurements taken at regular intervals.

One of the most important reasons for doing time series analysis is to try to forecast future values of the series. A model of the series that explained the past values may also predict whether and how much the next few values will increase or decrease. The ability to make such predictions successfully is obviously important to any business or scientific field.

The Time Series Modeler procedure estimates exponential smoothing, univariate Autoregressive Integrated Moving Average (ARIMA), and multivariate ARIMA (or transfer function models) models for time series, and produces forecasts. The procedure includes an Expert Modeler that automatically identifies and estimates the best-fitting ARIMA or exponential smoothing model for one or more dependent variable series, thus eliminating the need to identify an appropriate model through trial and error. Alternatively, you can specify a custom ARIMA or exponential smoothing model

2.1 Exponential smoothing models

Exponential smoothing is simply an adjustment technique which takes the previous period's forecast, and adjusts it up or down based on what actually occurred in that period. It accomplishes this by calculating a weighted average of the two values.

The following notation is specific to exponential smoothing models where:

- α is the level smoothing weight (which ranges from 0 to 1) i.e weighting factor
- γ is the trend smoothing weight (actual value)
- δ is the damped trend smoothing weight
- δ is the season smoothing weight
- t is the current time period

The estimation and forecasting of the exponential smoothing is the sum of the squares of the one-step ahead prediction error, $\sum (Y_t - \hat{Y}_{t-1}(1))^2$ is minimized to optimize the smoothing weights

Simple exponential smoothing has a single level parameter and can be described by the following equations:

$$L(t) = \alpha Y(t) + (1 - \alpha)L(t - 1)$$

$$\hat{Y}_t(k) = L(t)$$

$Y(t)$ is multiplied by α and $(1 - \alpha)$. If we keep on substituting the forecasted values, the historical data (actual values) is weighted exponentially. That is why this method is called exponential smoothing.

Holts exponential smoothing has level and trend parameter and can be described by the following equations:

$$L(t) = \alpha Y(t) + (1 - \alpha)(L(t - 1) + T(t - 1))$$

$$T(t) = \gamma(L(t) - L(t - 1)) + (1 - \gamma)T(t - 1)$$

$$\hat{Y}_t(k) = L(t) + kT(t)$$

Brown's exponential smoothing has level and trend parameters and can be described by the following equations:

$$L(t) = \alpha Y(t) + (1 - \alpha)L(t - 1)$$

$$T(t) = \alpha(L(t) - L(t - 1)) + (1 - \alpha)T(t - 1)$$

$$\hat{Y}_t(k) = L(t) + ((k - 1) + \alpha^{-1})T(t)$$

Damped –Trend exponential smoothing has level and damped trend parameters and can be described by the following equations:

$$L(t) = \alpha Y(t) + (1 - \alpha)(L(t - 1) + \phi T(t - 1))$$

$$T(t) = \gamma(L(t) - L(t - 1)) + (1 - \gamma)\phi T(t - 1)$$

$$\hat{Y}_t(k) = L(t) + \sum_{i=1}^k \phi^i T(t)$$

Simple seasonal exponential smoothing has level and season parameter and can be described by the following equations:

$$L(t) = \alpha(Y(t) - S(t - s)) + (1 - \alpha)L(t - 1)$$

$$S(t) = \delta(Y(t) - L(t)) + (1 - \delta)S(t - s)$$

$$\hat{Y}_t(k) = L(t) + S(t + k - s)$$

Winters' Additive exponential smoothing has level trend and season parameter and can describe by the following equations:

$$L(t) = \alpha(Y(t) - S(t - s)) + (1 - \alpha)(L(t - 1) + T(t - 1))$$

$$T(t) = \gamma(L(t) - L(t - 1)) + (1 - \gamma)T(t - 1)$$

$$S(t) = \delta(Y(t) - L(t)) + (1 - \delta)S(t - s)$$

$$\hat{Y}_t(k) = L(t) + kT(t) + S(t + k - s)$$

Winters' multiplicative exponential smoothing has level, trend and season parameters and can be described by the following equations:

$$L(t) = \alpha(Y(t)/S(t - s)) + (1 - \alpha)(L(t - 1) + T(t - 1))$$

$$T(t) = \gamma(L(t) - L(t - 1)) + (1 - \gamma)T(t - 1)$$

$$S(t) = \delta(Y(t)/L(t)) + (1 - \delta)S(t - s)$$

$$\hat{Y}_t(k) = (L(t) + kT(t))S(t + k - s)$$

3. DESIGN OF MARKETING PREDICTIVE ANALYTICS METHODOLOGY

The study has drawn upon recent studies of SMEs; from IHS proprietary data and reports; and most significantly from primary research of SMEs through an online survey.

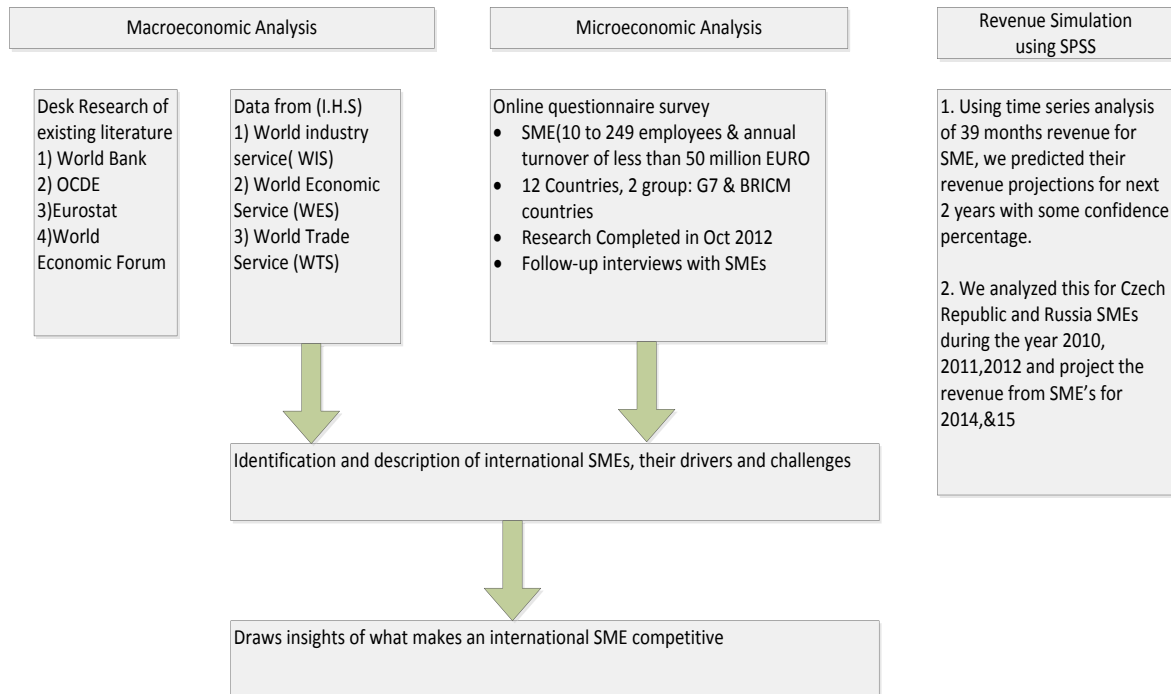


Figure 1. Approach of Marketing Predictive Analytics Methodology.

Source: Author & I.H.S Survey. Note: The SME sample for the primary research is based on 410 respondents – owners or members of the senior management team at SMEs having between 10 and 249 employees. The questionnaire is available with the author upon request.

4. PERFORMANCE INDICATORS

We identified a group of high-performing SMEs based on their average annual growth rate over last three years. These were defined as SMEs who have achieved:

More than 10% average annual growth rate over last three years for G7 countries (on average, the G7 countries had a 1.58% growth in GDP). More than 20% average annual growth rate over the last three years for BRICM countries (on average, the BRICM countries had a 5.84% growth in GDP). The study also classified SMEs by key competitive advantage; were they “efficiency” or “innovation” driven. Of course, all SMEs have a mix of both criteria but, through our research, we were able to classify two groups according to their predominant business characteristic. Efficiency-driven companies compete on the basis of efficient production processes, quality product improvements and well-organized logistics services. Innovation-driven companies compete by providing new or unique products / services creating their own market

5. REVENUE ANALYSIS METHODOLOGY

We performed several revenue analyses with various statistical methods and based on different customer segmentations (e.g. customer classification according to the industry or loyalty codes) to receive the prediction with the highest possible quality.

In the end we selected three methods with the best performance across Mexico.

1. Prediction of total revenue
2. Separate predictions of mean revenue per invoice and
3. number of invoices, for the whole SME sector together

The fitting of the time series and the predictions were created in SPSS Modeler with Expert Modeler function

5.1 Process

- 1) We used customer relationship management (CRM) to gather information about customers for the countries (Mexico) along with their account number.
- 2) Each customer is uniquely identified and may have many account number associated.
- 3) The revenue per month aggregated by account number for each country for last 40 months

We identified the SME customer segment based on the revenue and run the SME revenue analysis. Also the clustering with SME was based on the following

- a. Sales channel –it is defined as “A channel to market is the method of getting your product into the customer’s (the end user’s) hand. This can either be through direct sales, or through a reseller.”
- b. Loyalty Code – it is defined as “Customer loyalty is all about attracting the right customer, getting them to buy, buy often, buy in higher quantities and bring you even more customers”

The following value was predicted using the time series model

- 1) Prediction of total revenue
- 2) Prediction of mean revenue per invoice and of number of invoices

The quality of the model could be improved if the total revenue was divided into 2 individual time series:

Total revenue = number of invoices * mean revenue per invoice.

The number of invoices and the mean revenue per invoice are then analysed separately. This brings new insight into the revenue analysis, because the series usually behave differently and this knowledge can be integrated into the further decision process (e. g., although the total revenue is constant, the mean revenue is decreasing while the number of invoices is rising).

The primary reason to analyse total revenue by number of invoices and mean invoice per invoice is if the customer sends more shipments with less volumetric weight in future very frequently, then the company will have increase in the number of invoices but with less revenue owing to decline in the volumetric weight. So during forecasting, mean revenue per invoice was also taken into consideration and its future value was also predicted to ensure that revenue increase even if the number the invoices increases.

6. EMPIRICAL RESULTS & ANALYSIS

Our first group of interests in international SME that operation in two or more countries; typically 70% of country respondents

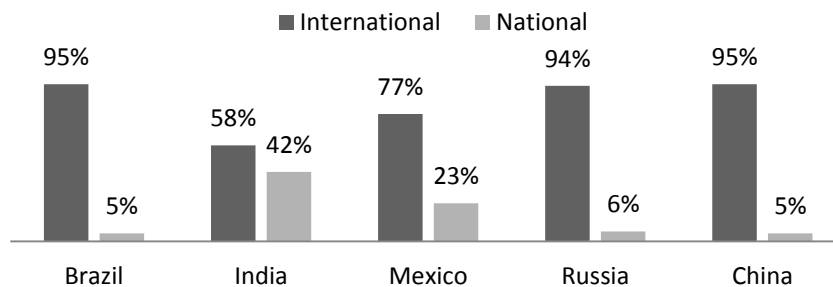


Figure 2 – Graph representation of International SME Operation in 2 or more countries
Source: I.H.S Survey 2012

7. INTERNATIONAL SMES HAVE DEVELOPED MULTI-FACETED INTERNATIONAL ACTIVITIES

Small and medium-sized enterprises are affected by globalization while being increasingly forced to think and act internationally. The first finding of this study is that SMEs' internationalization no longer has a limited focus on exporting / importing, but has become a much more differentiated business activity encompassing subcontracting as well as technical or commercial cooperation. SMEs may be engaged in cross-border partnerships and foreign investments to capitalize on new opportunities.

Although smaller SMEs are less internationalized than bigger SMEs, but even for them, internationalization is today a reality. While 80% of SMEs with 50 to 249 employees are operating at an international level, 66% of SMEs with 10 to 49 employees are international. One point to notice nevertheless is that the size difference is still marked when analyzing the share of small-sized enterprises with more complex forms of internationalization, or a combination of more than one form of internationalization.

The modern SME may well be engaged in international business activities beyond IMPORT/EXPORT

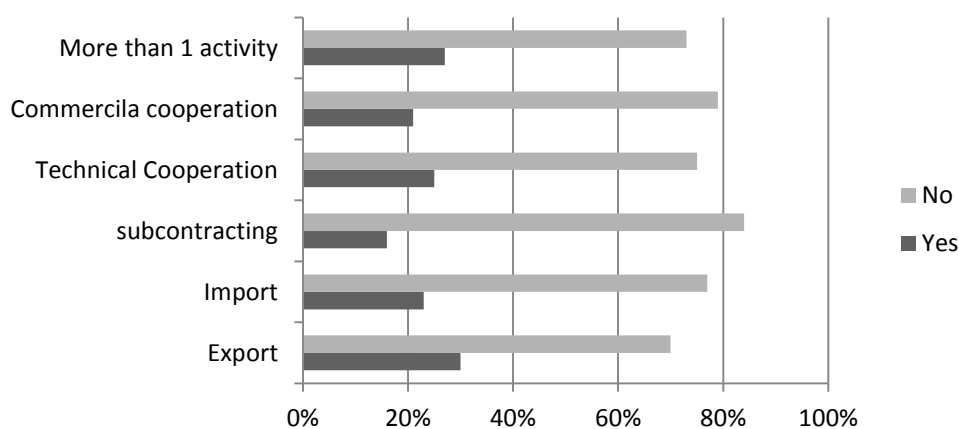


Figure 3: Percentage of SME's involved in international business activities
Source: I.H.S Survey 2012. Note: Technical cooperation defined for example, sharing know-how technologies etc. Commercial cooperation defined as marketing, distribution etc.

Our survey identified a high number of SMEs having international activities within their first five years of existence. For instance, while 27% of all SMEs have more than one international activity, this indicator rises to 31% of SMEs with less than five years of trading, despite having had less time to expand their businesses (a general assumption would likely be that the figure would be much lower for younger SMEs). This demonstrates a growing trend towards the internationalization of SMEs.

Young international SMEs are a reality of today's economy and are, in our survey, responsible for an important part of SME internationalization. Recent literature points to a growing number of such firms trading internationally within the first five years of their creation. These 'born global' SMEs see themselves as international rather than national players.

Interestingly, these 'born global' SMEs are also more prevalent in BRICM countries (24%) than in G7 countries (13%). The rationale behind could be that BRICM based small and medium-sized enterprises are strategically more focused on international markets than their G7 peers.

8. LOGISTICS SERVICE

A World Bank study on logistics performance - "Connecting to Compete" - includes an index built around a survey of logistics professionals who evaluate the logistics environment in the countries where they work, providing information on the quality of infrastructures, the performance of core services, the ease of trade clearance procedures, and the time, cost, and reliability of import and export supply chains

The table below shows the logistics performance index (score) for BRIC+M.

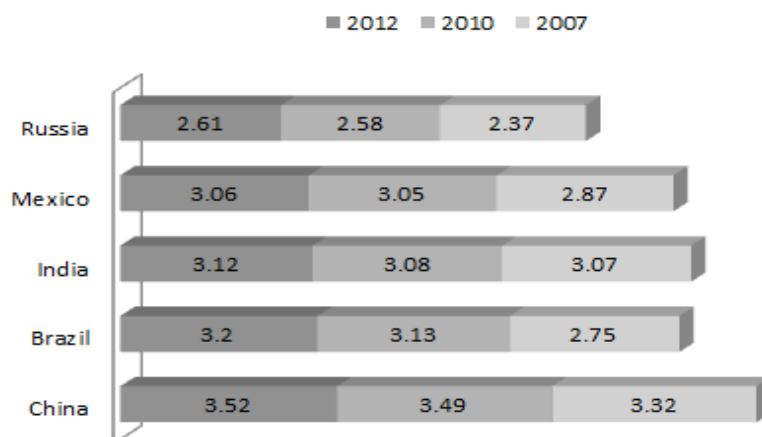


Figure 4: Logistics Performance Index Logistics performance index: Overall (1=low to 5=high)

Source: World Bank (2007 to 2012)

Logistics Performance Index overall score reflects perceptions of a country's logistics based on efficiency of customs clearance process, quality of trade- and transport-related infrastructure, ease of arranging competitively priced shipments, quality of logistics services, ability to track and trace consignments, and frequency with which shipments reach the consignee within the scheduled time. The index ranges from 1 to 5, with a higher score representing better performance. The data is derived from Logistics Performance Index surveys conducted by the World Bank in partnership with academic and international institutions, and private companies/ individuals engaged in international logistics. The 2009 round of surveys covered more than 5,000 country assessments by nearly 1,000 international freight forwarders. Respondents evaluate eight markets on six core dimensions on a scale from 1 (worst) to 5 (best). The markets of the respondent's country are chosen based on three considerations; the most important export and import markets, random selections, and, for landlocked countries, neighbouring countries that connect them with

international markets. Scores for the six areas are averaged across all respondents and aggregated to a single score using principal components analysis. Details of the survey methodology and index construction methodology are in Arvis and others' *Connecting to Compete 2010: Trade Logistics in the Global Economy* (2010).

For BRICM SMEs logistics are seen as having a strong positive effect on their business performance

The table below shows the percentage of G7 SMEs and BRICM SMEs that consider logistics as having a “strong positive effect” on their business performance. BRICM SMEs consistently value logistics services higher than their G7 peers, often to a factor of 2 or more. On average, 14% of G7 SMEs consider logistics services as fundamental to their strong business performance compared with 27% of BRICM-based SMEs.

Table 1. What effect do you think logistics can have on the following aspect of your business performance?

Business Performance	SME's	BRICM	
		SME's	G7 SME's
Increasing Sales	27%	38%	19%
Opening new markets	26%	38%	17%
Accessing new products, materials or suppliers	21%	31%	13%
Differentiating your products or service offering	20%	28%	14%
Reducing your need for long term capital	16%	21%	13%
Reducing Operating cost	15%	19%	12%
Reducing Stock obsolescence	14%	18%	11%

Source I.H.S survey 2012.

9. INTERNATIONAL COMPETITIVE ADVANTAGES - INTERNATIONALIZATION AS A DRIVER TO PERFORMANCE

Internationalization is seen as an opportunity to increase sales, while additionally affects the firm's competitiveness in other ways too. For instance, through improved cost-efficiency by subcontracting abroad; developing know-how and technology competencies via technical cooperation; and extending product ranges through commercial partnerships.

From our survey, we observe two interesting findings:

- For 41% of SMEs, the main reason to develop international activities is to access new markets.
- For 31% of our respondents, the main reason to develop international activities is linked to long term business growth ('Access to know-how and technology' and 'Diversification of product / service portfolio').

Table 2. Question: What are your main reasons to increase your international business activity?

Reason to increase international activities	International SME's
Access to new markets	41%
Access to know-how and technology	17%
Diversification of product/service portfolio	14%
Additional production capacity	11%
High labour cost in the domestic market	7%
Access to cheaper raw material	4%
Access to capital	3%
Access to labour force	2%
More flexible regulation	1%

Source I.H.S. survey 2012

Encouraged by initiatives from the World Trade Organisation (WTO) and the General Agreement on Tariffs and Trade (GATT), as well as regional agreements such as MERCOSUR and the EU Single Market, subcontracting, technical and commercial co-operation can strengthen the ability of SMEs to compete successfully at the international level while continuing to maximise their local strengths. One example of can be found in the northern Mexican regions. Small and medium-sized enterprises there have developed a specific form of cross border partnership that takes advantage of the innovative US business environment, allowing access to know-how and technology.

10. REVENUE ANALYSIS RESULT

The total revenue of Mexico shows rising trend with seasonality as well. All the models were of similar quality, so the simplest one – direct prediction of the total revenue – was chosen. According to this model, the revenue should increase from by 34.7% by 2015 when compared to 2012 revenue.

The following result is based on:

- SME’s monthly revenue from Jan 2010 to April 2013.
- The number of SME were 5,463 SMEs’ for Mexico.
- “Total_revenue_1” show the total revenue increase year on year with increasing trend and seasonality.
- “Total_revenue_2” shows the increasing and seasonal trend in the mean number of invoice.
- “Total_revenue_3” shows the increasing and seasonal trend in the number of invoices.

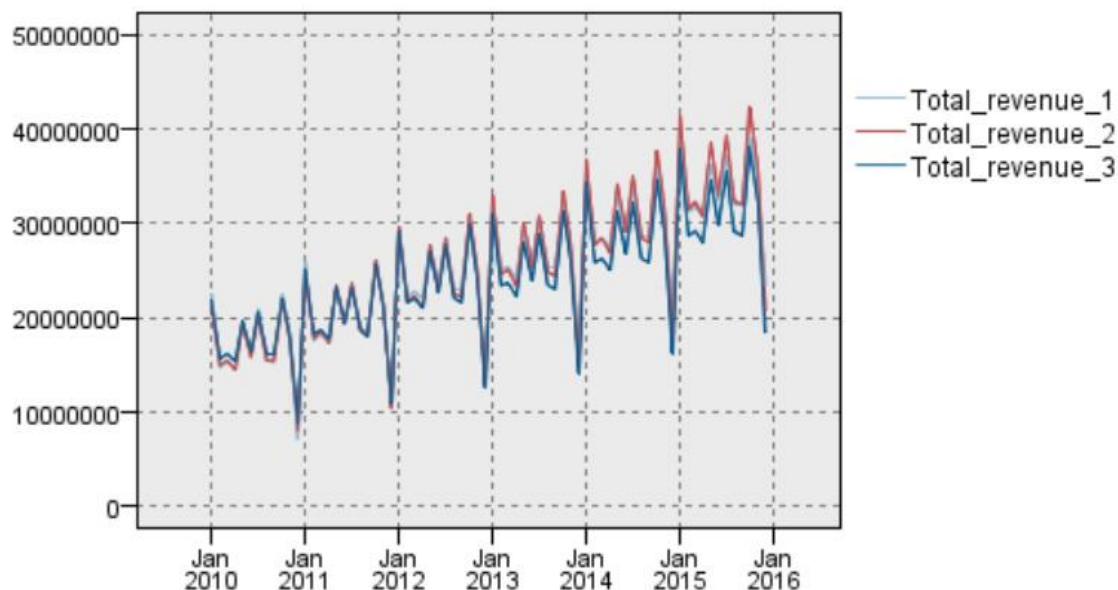


Figure 5. Comparison of the predicted SME’s total revenue calculated with 3 different methods for Mexico

Source: Author from revenue simulation

11. CONCLUSION

So, do SMEs that trade internationally perform better? Our research strongly suggests that they do.

We were surprised by the high proportion of our sample that traded internationally. Given this sample profile it is reasonable to expect that international SMEs figure significantly in our high-performers category; but they do outperform their domestic-only peers. So the idea of internationalization being a driver of business performance is certainly supported by our results.

The reasons for this could be that international SMEs transfer best practice developed internationally to their overall business, as well as the idea that SMEs which expand internationally are more likely to be ambitious.

Evidently, SMEs are increasingly integrated into the global economy and not limited to regional / national activities, but in fact have gone beyond what is often the first step of internationalization; exporting / importing. Among the SMEs surveyed, 73% of companies had at least one international activity and, among them, 43% were involved in exporting activities – SMEs are not just local service providers.

Further points of interest with regard to international SMEs which support our conclusion include:

International SMEs perform better than the average domestic SME; 26% of the international SMEs in the sample were high performers, while only 13% of the domestic-only SMEs were measured in that study. In fact, more than 30% of our respondents see the increase of their international activities as a way to improve their long term business growth through acquisition of knowhow and product diversification.

SMEs are increasingly focused on doing business internationally, with younger companies which are more likely to be engaged in overseas markets despite having had less time to grow their businesses. Often referred to as ‘born global’, these young international SMEs are a reality of today’s economy often exploiting the spread of inexpensive communication technologies and efficient logistics services.

SMEs in BRICM countries are more likely to have international activities than SMEs in G7 countries: one explanation for this is that a real business driver is to set up strong business relationships with high consumption per capita developed markets. In fact, 70% of BRICM high-performing SMEs have the majority of their international clients, partners and subcontractors in developed countries. This also suggests they are better placed to respond to opportunities in new geographical markets than many G7 SMEs in the future.

High-performing international SMEs cited three key challenges to their export efforts; ‘lack of knowledge of foreign markets’, ‘high customs duties in the destination country’ and ‘establishing contacts with foreign partners / customer base’. Governments looking to boost the competitiveness of their SMEs should take serious consideration to these factors.

Logistics is seen as having a positive effect on many aspects of a SME’s performance with a distinct difference between G7 countries (where logistics is seen as a way to reduce operating costs) and BRICM countries (where logistics is seen as a means to differentiate their product or service offering).

Finally, and impacting all SMEs, there is a real lack of reliable and up-to-date information about SMEs on a country by country basis, despite the significant contribution made by SMEs to employment (typically 35- 45% of total employment) and value added to an economy (typically 30-40% of total value added). This lack of information is itself a restraint upon SMEs since it restricts SMEs’ ability to organize them while present their case around credible data and information; basically to have a “voice.” Linking back to the internationalization thread of this report, as one respondent explained, banks, investors, institutions do not think of SMEs as operating at an international level. This is certainly in part due to the lack of reliable information on this subject which hinders the construction of a clear vision for such a heterogeneous group. Evidently to this report, there is a clear opportunity for policy makers to support this sector as a means to create more jobs, add value, and increase export earnings.

From the SPSS analysis, we could see that there is immense potential in SME sector, especially in Mexico. If we can provide portfolio of products designed for SME, we can activate this potential and increase the revenue of growth for the next couple years through predictions based on analysis of the past few years’ performances.

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ACCOUNTING POLICY VERSUS CREATIVE ACCOUNTING

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Abstract: *Accounting policy is a set of guidelines, regulations and rules selected from the applicable accounting law. The policy enables preparation of a company's financial statement that is of high quality and reflects its real situation. Proper selection of accounting policies could have an impact on some measurements of assets and financial performance of an entity, which may influence the decisions made by users of financial statement. However, an accounting policy cannot be used by entities as a means to arbitrarily benefit a company's financial position and therefor improve the image of a company compared to competition. Income-boosting accounting changes, income-smoothing accounting changes or non-disclosure of stakeholder relevant information could be considered fraud.*

The purpose of this paper is to present the significant role of accounting policy and its influence on the reported figures. By examining the financial statement of ABC Company the study portrays the range of accounting policies and highlights the difficulty of distinguishing accounting changes applied in order to enhance the credibility of information provided by the financial statement from deliberate adjustments in the book of accounts made with the intent of gaining advantages and meeting internal targets. Therefore, in order to facilitate understanding of the issue this study provides practical examples of some deliberate adjustments and indicate their direct impact on the financial statement.

Keywords: *accounting policy, creative accounting*

1. INTRODUCTION

The purpose of this paper is to present the significance of accounting policies as an instrument that affects financial statements of entities. The following research thesis has been assumed: Accounting policy is a mandatory element of accounting systems while being combined with multiple subjective assumptions and solutions applied by entities. As a result, the following research questions were formulated:

- What is accounting policy and what does it cover?
- How to set the limits between the development and implementation of modifications to accounting policies in order to make the financial statements more reliable as a source of information and adjusting the previously selected methods to the changing conditions, and conscious application of instruments of development and modifications to accounting policies in order to obtain the planned final effect?

Description of the accounting policies applied by an entity constitutes an integral part of a correctly functioning accounting system and the generated financial statements. The significance of accounting policies as an element of the accounting system is the fact that international, US and domestic regulations of many countries set different standards. The issues related to accounting policies are regulated *inter alia* in IAS 8 "Accounting policies, changes in accounting estimates and errors" and in SFAS 154 „Reporting Accounting Changes” (KPMG, 2005).

Accounting policies include a set of guidelines, standards and rules selected – subject to legislator's consent – from among the available solutions so that the financial statements generated on that basis are characterized with high quality and reflect the actual situation of the company with the highest possible extent of adequacy of the disclosed data. Therefore, such solutions need

to be selected within accounting policies that information and data disclosed in financial statements are reliable, comparable and material.

However, one of the core elements of accounting policies is the selection of specific rules and methods to measure assets and liabilities and to determine the financial result from among all solutions available in the applicable regulations on financial statements. The possibility of a reliable measurement of all assets, liabilities, income and expenses is a criterion to be complied with recognition of balance sheet elements in the books of account and disclosure thereof in the financial statements. An appropriate selection of accounting principles may affect the values of selected financial ratios (for instance liquidity or profitability ratio), on the decisions taken by readers of financial statements and in some instances – also on reduced tax liabilities or profit distributions to shareholders (Sawicki, 2000, p. 94).

Entities may not treat accounting policies as an instrument with which to create an improved financial condition of the entity against the background of competitors by manipulating, disclosing enhanced data or simply by omitting disclosures in the financial statements of data that may be material for readers of the financial statements.

2. CREATION OF ACCOUNTING POLICIES AND CREATIVE ACCOUNTING

As mentioned above, entities may select their accounting policies and may also elect to modify such policies subject to certain requirements. In accordance with IAS 8, entities may modify their accounting policies “only when this is required by provisions of the relevant standard or interpretation thereof; or when the result is that the information in the financial statements in the impact of transactions, other events or conditions on the financial condition, financial result or cash flows of the entities is more useful or reliable” (IAS 8, par. 14).

In accordance with art. 8.2 of the Accounting Act – in order to present the economic and financial condition of the company to the readers, the entity may modify the previously applied accounting principles departing from the applied consistency principle, as at the first day of a new financial year or apply modifications and restate balance sheet items in order to adapt the previously applied accounting policies (principles) and accounting estimates.

Modifications to accounting policies as listed above may for instance be a result of:

- modifications to the law and a need to make adaptations to comply with the regulations of the balance sheet law;
- the entity obtains a right to apply simplifications as provided for in the regulations on accounting or the entity loses such right;
- change of the objects or extension or limitation to the business objects of the entity;
- the need to adapt the entity to the solutions prevailing in its capital group of which the entity has become a member or the sectors in which it started operation;
- recommendation after financial inspections held in the entity;
- commencement or resignation from applying IAS/IFRS;
- a decision taken by the management of the entity to modify the principles for internal reasons (Accounting Standards Committee 7, item III.3.8).

It is a major problem how to set the limits between the development and implementation of modifications to accounting policies in order to make the financial statements more reliable as a source of information and adjusting the previously selected methods to the changing conditions, and conscious application of instruments of development and modifications to accounting policies in order to obtain the planned final effect. It is worth remembering that persons responsible for accounting in an entity are professionally and ethically liable for the objectivism and reliability of the information prepared and disclosed by them (SKwP, 2012). Assessing the introduced modifications, difficulties are often encountered in identifying the objectives and the correctness of the modifications as well as clear qualification of the underlying reasons. There are no doubts,

however, that activities lying beyond the area covering the statutory understanding of accounting policies and modifications thereto, should be classified as creative accounting.

In the literature on the subject, creative accounting is termed as abuse performed by business entities or persons aimed at unreliable presentation of data on economic and financial condition (Wąsowski, 2005, p. 10). Creative accounting may be then understood as irregularities in preparing financial statements of business entities or even as a synonym of accounting fraud (Kutera, Hołda, Surdykowska, 2006, p. 15).

However, some experts stress that creative accounting should not be associated only with negative accounting practices since it covers a much broader sphere than only those termed as accounting fraud (Surdykowska, 2005, p. 27). There are two core activities related to creative accounting:

- performed in line with the “spirit of the law”,
- unlawful (Kutera, Hołda, Surdykowska, 2006, p. 32).

Accounting activities performed in line with the spirit of the law are such that are aimed at selecting alternative solutions within accounting policies or modifying the earlier selected methods provided for in the Accounting Act or other applicable regulations. The activities of the other type being wilful misleading or intentional manipulation of the effect of the information should be termed as accounting fraud.

Accounting (financial) fraud may be defined as comprehensive and sophisticated falsification of financial statements that is done in secret to generate indirect or direct economic benefits. Thus, a conclusion can be drawn that financial fraud is a clearly negative notion while the assessment of actions of creative accounting depends on the type, scope, purpose and potential effects. Financial fraud is often associated with “white-collar crime” which is defined as crime without violence to generate financial benefits for people who have specialist, technical or other professional knowledge in business, central or local government affairs, or who have used their economic position, influence or trust within an organisation (Bela, Bolesławska, 2005, p. 19–20). The definition – as broad as it is – attributes the probability of the organisation as being the perpetrator while the government or the society at large are the harmed parties (Kranacher, Riley, Wells, 2011, p. 60).

The circumstances within which entities often decide to apply creative accounting techniques may occur for instance in a situation of pressure caused by market expectations or requirements of loan agreements (Świdarska, Więclaw, 2009, p. 1–16). As a result of data manipulation in financial statements, the generated image of the entity may be better or worse than it actually is. A more favourable image is created by overstating profit or asset value of the entity in order to attract investors, loans or to maintain the stock prices at a high level. A reverse situation which is an intentional presentation of a worse situation of an entity occurs when for instance the entity wishes to show growth dynamics in the future, avoid paying dividend to its shareholders, justify headcount reduction or artificially understating the value of the organisation so that additional benefits can be generated when the company is purchased (Wąsowski, 2005, p. 9–10). According to P. Tickner, a manager who is remunerated in line with the results of the company, both directly in the form of bonus or indirectly in the form of promotion, will most often be “tempted” to manipulate data to their benefit (Tickner, 2010, p. 41). Michael R. Young goes even further, stating that the existing system of interim financial reporting exerts pressure on honest employees to commit financial fraud (Young, 2006, p. 363).

When financial statements are made that are expected to generate an assumed effect, instruments are used that may be qualified to two basic forms of balance sheet policies as follows (Cebrowska, 2010, p. 230):

- material balance sheet policy that may affect the financial result,
- formal balance sheet policy which determines the structure, presentation and grouping of specific items of the financial statements.

Entities have two options within accounting policies within the two above groups – an appropriate selection of solutions or a modification to accounting policies may be called in these circumstances

an instrument of balance sheet policy that is used to accomplish pre-determined objectives.

Classical techniques applied within the area of creative accounting related primarily to: premature recognition of income, disclosure in the books of account of non-existent income, overstating income by including one-off profit, transfer of the costs of the current reporting period to subsequent periods, failure to disclose all liabilities, postponing current income to subsequent periods and recognition within the current period of costs that apply to future periods. Although such classical instruments used in creative accounting are commonly known, the persons creating the image of the entity may demonstrate a range of various ideas and solutions to justify and argue in favour of specific decisions related to books of account what as a result are difficult to challenge by persons controlling the entity. Therefore, proving irregularities related to the use of a specific creative accounting technique or instrument poses a major challenge to auditors in certain instances.

However, the addressees of information provided in financial statements – although theoretically they may expect that Polish legislation and regulatory institutions will reduce room for manipulation and falsification of financial statements by management of companies – should be cautious taking decisions on the basis of such disclosed information (Surdykowska, 2005, p. 26). Special attention to the data disclosed in financial statements should be paid by those who intend to take investment decisions on that basis.

Generally speaking, it is hard to state without any doubt that creative accounting technique are wrong – it is the intentions of persons applying them and the scale of such application determine their true nature and justification (Syed Zulfiqar Ali Shah, Safdar Butt, 2011).

3. WHAT DOES ACCOUNTING POLICY COVER – THE CASE STUDY ON THE BASIS OF THE FINANCIAL STATEMENTS OF THE ABC COMPANY

The ABC Company is a polish joint stock company which shares are not open to the public offer. The company develops financial and accounting software for small and medium-sized enterprises, offers accounting services (keeping the accounts, revenue and expenses ledger) and offers legal and business consulting and IT advices.

The analyzed non-consolidated financial statement of the ABC Company for the year 2011 was prepared in accordance with the Accounting Act. The independent external auditor gave unqualified opinion. Tables 1. and 2. present short-forms of the balance sheet and the profit and loss account of the ABC Company for the year 2011.

Table 1. Balance sheet of the ABC Company in PLN (31.12.2011)

ASSETS		31.12.2010	31.12.2011
A.	Non-current assets	1 073 085,24	1 929 746,29
I.	Intangible assets	90 616,67	1 032 733,33
II.	Tangible fixed assets	366 875,53	358 025,76
III.	Long-term receivables	0	0
IV.	Long-term investments	614 523,82	538 908,98
V.	Long-term prepayments and accruals	1 069,22	78,22
B.	Current assets	1 538 355,77	1 813 284,03
I.	Inventories	14 349,23	14 017,61
II.	Short-term receivables	547 298,44	431 214,76
III.	Cash and cash equivalents	968 716,69	1 359 979,63
IV.	Short-term prepayments and accruals	7 991,41	8 072,03

Total assets		2 611 441,01	3 743 030,32
EQUITY AND LIABILITIES		31.12.2010	31.12.2011
A.	Shareholders' equity	2 326 445,29	2 921 419,83
I.	Share capital	500 027,00	500 027,00
II.	Reserve capital	1 779 384,88	1 497 464,81
III.	Revaluation reserve	328 953,48	278 056,36
IV.	Net profit (loss)	-281 920,07	645 871,66
B.	Liabilities and reserves	284 995,72	821 610,49
I.	Reserves	0,00	129 396,00
II.	Long-term liabilities	0,00	28 028,98
III.	Short-term liabilities	284 995,72	322 185,51
IV.	Accruals	0,00	342 000,00
Total equity and liabilities		2 611 441,01	3 743 030,32

Table 2. Profit and loss account of the ABC Company for the year 2011 (in PLN)

Figures		01.01.2010-31.12.2010	01.01.2011-31.12.2011
A.	Sales revenues	2 515 049,39	3 111 648,13
B.	Manufacturing cost of products, goods and services sold	2 256 480,13	1 732 995,05
C.	Gross earnings from sale	258 569,26	1 378 653,08
D.	Cost of sale	63 504,73	110 398,04
E.	Cost of general management and administration	576 764,77	620 201,85
F.	Earnings from sale	-381 700,24	648 053,19
G.	Other operating income	79 867,43	112 207,92
H.	Other operating expenses	27 087,19	12 300,57
I.	Profit on operating activity	-328 920,00	747 960,54
J.	Financial revenues	63 068,82	71 678,25
K.	Financial costs	16 068,89	30 950,13
L.	Profit before tax	-281 920,07	788 688,66
M.	Income tax	0,00	142 817,00
N.	Net profits (loss)	-281 920,07	645 871,66

The biggest shares of the Company's fixed assets are long-term investments and tangible fixed assets. Most tangible fixed assets include buildings, lands and vehicles. Long-term investments consist primarily of long-term financial assets which include shares and stocks in subsidiaries and other companies. Current assets include most of all short-term receivables and short-term investments (cash and cash equivalents). When it comes to the shareholders' equity – it accounted for 78% of total equity and liabilities. Current liabilities were the biggest share of the total liabilities in the year 2011.

In 2011 the ABC company's sales revenue were coming mostly from the sales of accounting services – 49%, IT services – 22% and the sales of software and licenses – 27%. Main

operating expenses were salaries and external services.

Solutions within accounting policies selected by the ABC Company are described in the introduction to the financial statements and other additional documentation (corporate chart of accounts, accounting policies, accounting policies annexes, appendices, resolutions of the board of directors). The section below discusses the most important aspects related to accounting policies applied by the ABC Company.

Materiality threshold

The ABC Company has adopted materiality threshold for its balance sheet at the level of 2% of the total assets (i.e. 74 860, 61), and for the profit and loss account at 1% of the revenue (i.e. PLN 6 458.72). It is assumed that no amount below the materiality threshold substantially affects the shape of the financial statements, and should not mislead the recipients. Determination of materiality threshold is permitted under the Accounting Act – an entity may apply simplifications as long as it has no negative impact on clear and fair presentation of the financial position and financial results of the company (Accounting Act of 1994, Art. 4). The effects of such action primarily come down to reduction in the level of detail of data presented.

Depreciation write-downs – intangibles

Company's intangibles consist primarily of licenses, software and IT platforms. Last year, intangible assets accounted for only 8% of the fixed assets, while in 2011 this share increased to 53%. The ABC Company has adopted the following rates of depreciation for its intangibles: 50% (concessions and licenses), 20% (software) and 12.50% (others). In 2011 depreciation write-downs regarding intangibles amounted to PLN 25 883.34, which accounted for 30% of all depreciation costs incurred by the entity.

Depreciation write-downs – fixed assets

Tangible fixed assets of the Company under the discussion consist primarily of buildings and vehicles. The Company has adopted the straight-line method of depreciation of fixed assets, and the commencement of depreciation takes place in the month following the adoption of the fixed asset for use. Examples of depreciation rates applied include 2.5% and 10% (buildings), 10 and 20% (equipment and machinery) and 20% (means of transport). In 2011, depreciation write-downs of tangible fixed assets amounted to PLN 62 709.77, of which almost 60% was made up by depreciation of buildings, and this is precisely why the terms of depreciation of that part of the total assets exert a significant impact on the financial statements of the entity. Means of transport came second in terms of write-downs (28%). Other write-downs involved machinery and equipment and other fixed assets.

Depreciation solutions may be an accounting policy instrument that affects the shape of the financial statements. In the case of the analyzed entity this primarily involves depreciation of buildings and means of transport. The scale of the potential impact on the financial statements resulting from manipulation of depreciation rates depends on the share of tangible fixed assets in balance sheet total as well as the nature thereof. In the case of the Company under the discussion any changes in depreciation of means of transport could be quite difficult due to the fact that the adopted twenty percent rate is widely used and supported by the tax regulations. The situation could be different in the case of companies with a lot of machinery or equipment, or with rare equipment, as in such cases the possibility of adjustment of depreciation rates is much greater, and due to the occurrence of some machinery being "rare", it is more difficult for an auditor to undermine such rates and demonstrate irregularities of such potential changes.

Long-term investments

Long-term investments are an important component of the Company's and as at 31.12.2011 their total value amounted to PLN 0.5 mil. Therefore it appears adequate to say that methods adopted for the purpose of valuation of these assets will be a major factor in the shaping of the financial

statements. Table 3 shows the financial figures connected with the Company's long term investments.

Table 3. Long-term investments of the ABC Company

Long-term investments of ABC Company	31.12.2010	31.12.2011
Value	PLN 614 523,82	PLN 538 908,98
Share in fixed assets	57%	30%
Share in assets total	24%	14%
therein long-term financial assets	100%	100%
therein shares and stocks	100%	100%
therein in subsidiaries	24%	24%
therein in other companies	76%	76%

Most long-term financial assets include shares and stocks in other companies, with shares held subsidiaries representing 24% of that value. Under the existing regulations, shares and stocks should be assigned to one of three groups: the shares (stocks) held for trading, shares available-for-sale and shares in subsidiaries. In the case of the ABC Company all shares in other companies belong to the group of shares available-for-sale. The value of shares available for sale should be estimated on the balance sheet date at fair value (in the case of shares/stocks listed on a regulated market or shares/stocks whose fair value can be otherwise reliably determined) or at the cost less accumulated impairment write-downs (in the case of the remaining shares/stocks available for resale) (Regulation of Minister of Finance, 2001, Articles 14 and 16). An entity can recognize the effects of valuation only its financial result otherwise recognise the same in the revaluation reserve (Regulation of Minister of Finance, 2001, art. 21). As part of its accounting policy the Company has chosen the latter method, recognizing the effects of valuation in the revaluation reserve. As a result of choosing this method the effects of fluctuations in the value of shares do not result in significant changes in the financial result. For example, in 2008 – i.e. the year of the stock market crash, the shares held by the Company lost a substantial part of their value, however, due to the fact that the surplus from the previous periods were recognized in the revaluation reserve, this did not negatively affect the financial result.

In accordance with the Company's accounting policy, in the event there is evidence pointing to impairment of shares, the Company recognizes an impairment write off. In the event of a loss - the effects are recognized in the profit and loss account, however, if the revaluation of assets was previously recognized in the revaluation reserve – the value of revaluation reserve is reduced, and only the remaining part of the loss is reflected in the profit and loss account.

In accordance with the Accounting Act, a company valuate shares in subsidiaries at fair value or acquisition cost less accumulated impairment or in accordance with the equity method (Accounting Act of 1994, Art. 28, paragraph 1). In accordance with the adopted accounting policy the company estimated the value of shares held in subsidiaries at the acquisition cost less possible impairment. Estimates associated with shares in subsidiaries and affiliates are made using estimation methods commonly recognized as valid, which means building on premises showing the financial condition of the subsidiaries and affiliates.

The effects of the adopted accounting policy in terms of valuation of long-term investments included:

- revaluation write-down of PLN 28 988.43 (shares in affiliates)
- effects of revaluation of fair value recognized in the revaluation reserve amounted to PLN 50 897.12
- the reported period's financial income amounted to PLN 2 450.00
- the reported period's financial costs increased by PLN 27 167.72
- the value of long term financial assets decreased by 75 614.84

Valuation of Inventories

In accordance with the Company's accounting policy for inventories – the value of materials and goods is assessed based on the purchase price, while disbursements are valued according to the FIFO method. Costs incurred at the time of purchase of goods and materials are considered as insignificant and are recognized as expenses in the period they are incurred. Due to the fact that the value of the inventories is relatively low (0.5% the balance sheet total) the adopted accounting policy for their valuation does not significantly affect the outlook of the financial statements. It should however be noted that the valuation of inventories of other companies can be a very important factor affecting the outlook of financial statements - especially in the case of manufacturing companies, whose value of inventories at the balance sheet date is very significant, as well as companies whose inventories value is dependent on external factors, and fluctuates throughout the year.

Short term receivables revaluation write downs

The Company recognizes revaluation write downs on receivables, if it is highly probable that a debt might not be paid, moving the revaluation write down to operating or financial expenses. In 2011, the entity recognized depreciation write-downs on receivables overdue more than 180 days. The value of revaluation write down of trade receivables amounted to PLN 8 085.36, which accounted for only 2% of the short-term receivables. In the previous year the company recognized a receivables write-down of PLN 25 896.82, which was accounted for as a loss. However, in 2011 the company dissolved the revaluation write down, thus increasing operating revenue. The recognition and the subsequent dissolution of a revaluation write down did not distort the image in the long-term, nevertheless these facts did have an impact on the amount of profit or loss in the period 2010-2011.

Provisions for accounts payable

According to the Accounting Act, companies are obliged to recognize provisions for certain or highly probable future liabilities, the value of which can be reliably estimated (Accounting Act, 1994, Art. 35d.1.). The analysed financial statements contained a provision for bonuses for the Management Board of PLN 129 396.00. No such provisions were recognized in the past. This provision resulted in a 20% reduction of the 2011 net profit. The Company did not recognize any provisions for restructuring or warranty repairs. The Company estimated its retirement severance payment liabilities using estimation methods based on comparison with previous years. Due to the small amount of estimated liabilities – i.e. only PLN 3 600 and adopted the materiality threshold, this liability item is not reflected in the company's balance sheet. The ABC company does not offer long term service bonuses. As for other future liabilities - the notes to the financial statements contain a reference to an expected auditor's remuneration of PLN 7 000, for which no provision was recognized, as the value does not exceed the materiality threshold.

Interest income

According to the assumptions made by the ABC S.A. company, interest income is recognized in the accounts as the interest accrues. In determining the value of interest income the company uses an effective interest rate. Effective interest rate is the rate that takes into account the periods of capitalization of interest, the repayment method and any additional charges. As a result of the application of this interest rate, the estimated interest income is higher than the one estimated using the nominal interest rate, in the event that the interest payments are paid more than once a year. In 2011 the interest income of the ABC company amounted to PLN 50 217.35, of which 46 122.45 was interest income received, and PLN 4 094.90 payable interest with maturity period 3 months.

Transactions with affiliates

The Company's goods and products sales revenue to affiliates amounted to over PLN 866 000, which amounts to as much as 28% of the total sales revenue. As far as transactions with affiliates

are concerned the company applies the method of comparable uncontrolled price to estimate transfer prices. The method of comparable uncontrolled price involves comparison of prices in transactions between affiliated companies, with those applied in transactions between independent entities to determine the market value of the transaction (Regulation of Minister of Finance, 1997, art. 4, clause 1). Although the selected method does not significantly affect the valuation of transactions, and thus the financial result, but a large number of transactions involving affiliates has qualitative effects on information prepared – the company is required to prepare a comprehensive supporting documentation confirming the reliability and accuracy of valuation of these transactions.

Selection of profit and loss account variant and cash flow report

The company prepares the multi step variant of profit and loss account, while cash flow report is in line with the indirect method. The selection of variant for the preparation of an item of financial statements has a qualitative impact on the financial statements – i.e. it determines the type of data presented and the type of classification. If the method of preparation of the profit and loss account is changed, it will also result in changes to the distribution and presentation of the operating costs, which may have relevance to individual recipients of the financial statements.

Other aspects of the company's accounting policy

The documentation prepared by the Company contains a lot of additional information in the field of accounting policy concerning such issues as: the length of financial year, the capital accounts plan, the method of allocating costs to individual departments and products, computer programs used, data archiving methods, the manner of protection of documents and accounting records, the methods of settlement of prepayments and accruals, changes in accounting policies resulting from the implementation of projects co-financed from EU funds, the moment of recognition of revenues and dividends and the accounting treatment of leased assets. The above accounting policy issues were not analyzed due to their relatively small importance in the shaping of the financial statements.

Assessment of the significance of the accounting policies' aspects in the context of the financial statements creation

In conclusion, taking into account business economic activity of the Company and the percentages of the individual items of the financial statement – some of the aspects of the accounting policies can be identified that have a particular impact on the reported figures. That would include inter alia: adopted rates of depreciation for its intangibles, buildings and vehicles, shares and stocks' valuation methods (in subsidiaries and in other companies), estimates related to the write-downs of receivables, provisioning policy as well as valuation and documentation related to transactions with subsidiaries (especially for public inspection supervisors). Adopted methods for the inventory valuation, international transactions settlement and the valuation of assets and liabilities in foreign currencies have relatively low influence on the figures reported in the financial statement.

Worth taking into consideration is the fact that the significance of some accounting policies methods in the context of the financial statements developing may change according to the shares of some balance sheet items in the assets total and the scope of their influence on the profits.

4. CREATIVE ACCOUNTING TECHNIQUES – THE ABC COMPANY CASE STUDY

Prior section indicates accounting policies adopted by the ABC Company and their influence on the financial reports. The study below portrays some examples of techniques (deliberate adjustments in the book of accounts) using accounting policies as an instrument that affects the financial statement of the entity in order to obtain planned final effects. For the purpose of the analysis some accounting policies methods applied by the Company were changed and some

estimates and assumptions were made. The changes' potential impacts on the reported figures and the image of the economic and financial condition of the Company were indicated. While creating assumptions for the following analysis a number of simplifications were made and some of the calculations were estimated approximately. The Table below presents the examples of some changes in the area of accounting policies and their influence on the particular parts and items of the ABC Company's financial statement.

Table 4. The examples of changes in the accounting policies area and their impact on the financial statement of the ABC Company

No.	Activity	Value (PLN)	Impact on the balance sheet		Impact on the profit and loss account		Impact on the profits	Impact on the total assets
			Balance sheet's item	+/-	Profit and loss account's item	+/-		
1.	Recognition of a provision for the examination by an auditor	7 000	Equity and liabilities: provisions for liabilities	+	Operating costs	+	-	None
2.	Recognition of a provision for retirement benefits	3 600	Equity and liabilities: provisions for liabilities	+	Operating costs	+	-	None
3.	Resignation of the recognition of the provision for the Management Board' bonus	129 396	Equity and liabilities: provisions for liabilities	-	Operating costs: costs of general management	-	+	none
4.	Recognition of higher depreciation write-downs of the intangibles	15 000	Assets: Intangibles	-	Operating costs	+	-	-
5.	Decrease of the intangibles depreciation write-downs	5 000	Assets: Intangibles	+	Operating costs	-	+	+
6.	Decrease of the short-term receivables revaluation write-downs	5 300	Assets: short-term receivables	+	Other operating expenses	-	+	+
7.	Increase of the short-term receivables revaluation write-downs	12 525	Assets: short-term receivables	-	Other operating expenses	+	-	-
8.	Classification of the invoice for the renovation as for the modernization	15 500	Assets: tangible fixed assets	+	Operating costs: outsourced services	-	+	+
9.	Increase of the long-term investments revaluation write-downs	12 000	Assets: long-term investments	-	Financial costs	+	-	-

10.	Decrease of the long-term investments revaluation write-downs	10 000	Assets: long-term investments	+	Financial costs	-	+	+
11.	Recognition of the next period's costs as the costs of the current reporting period	10 000	Assets: short-term prepayments and accruals	-	Operating costs: advertisement costs	+	-	-
12.	Recognition of the next period's revenues as the revenues of the current reporting period	14 800	Equity and liabilities: accruals	-	Operating revenues	+	+	None
13.	Recognition of a provision for the expected losses arising out of the credit facility guarantee	120 000	Equity and liabilities: provisions for liabilities	+	Financial costs	+	-	None
14.	Accounting policy regarding research and development works	16 000	Assets: Intangibles	+	Operating costs	-	+	+

If the Company had not decided to accept a certain materiality threshold for its financial statements, it would recognize a provision for examination by auditor and a provision for retirement benefits. The recognition of the above indicated provisions would increase the reported period's operating costs by PLN 10 600.00, which would reduce the profit, with an unchanged balance sheet total.

During the analyzed periods the Company, for the first time, recognized a provision for a bonus payable to the Management Board. As the value of the provision is quite significant as compared to the other outcome values, the decision to recognize it had a significant impact on the financial result. If, as it was the case in previous years, this provision had not been recognized for particular reasons, the value of operating costs (overheads) would have been reduced, while the profit would have increased by PLN 129 396.

If the company was able to demonstrate that its intangibles are likely to generate benefits at a point of time different than initially assumed, it could verify its assumptions, thus resulting in verification of the revaluation write downs. Intangibles held by the company posted a significant increase during the reported period, and the Company could recognize higher depreciation write downs in the reported period. For the purpose of the analysis PLN 5 000 was assumed to be the value diminishing the value of intangible revaluation write downs, with PLN 15 000 was assumed to be the value increasing the previously assumed depreciation write downs. Increasing revaluation write downs would decrease the net value of the intangibles, increase the operating costs, thus resulting in lower profit. However, if it was decided to decrease the planned revaluation write downs, the changes would be quite opposite, i.e.: an increase of the balance sheet value of intangibles, a decrease in the value of operating costs and an increase in profit.

So far, the company recognized revaluation of short-term receivables overdue more than 180 days. However, the existing policy in this area (estimates) did not work in the previous period (in 2011, debts previously considered as bad, were repaid). It seems therefore possible that company could change the adopted methods for recognition of doubtful receivables. After analyzing the structure and the nature of the Company's receivables, it was considered feasible to reduce revaluation

write-downs by PLN 5 300, which would result in an increase in balance sheet receivables, a reduction in other operating costs and an increase in profit or loss and the balance sheet total. It was estimated that depreciation write downs could be increased by PLN 12 525, which would reduce the value of receivables, increase other operating expenses, profits the balance sheet total.

During the analyzed period the Company was invoiced for outsourced services valued at PLN 25 700. As the services in question were on the verge of renovation and modernization the company found it difficult to properly qualify the expenses. Ultimately the service was considered to be a renovation and the amount of PLN 25 700 was recognized as costs of the reported period. However the company could obtain appropriate documentation and split the amount in question into the individual services performed, and in consequence recognize the a part of that amount as renovation, and a part as modernization of the building in its possession. If 60% of the expense were recognized as modernization costs, then PLN would 15 500 increase the value of tangible fixed assets and would be depreciated in the future. Only the remainder of the expenses – i.e. PLN 10 200 would increase the current period's costs. Activation of the expenses incurred, would increase the analyzed period's profit and the balance sheet total.

It appears particularly difficult to assess the value and the legitimacy of the revaluation write downs on shares and stocks in affiliates. If the company had sufficient grounds, it could change its policy in this respect, and therefore the value of write downs in this respect. The amount of PLN 12 000 was found as a possible estimated value that could increase revaluation write downs on long term investments increasing the value of the period's financial costs, thus decreasing the company's profit and the balance sheet total. On the other hand decreasing of these write downs by PLN 10 000 would decrease financial costs, thus increasing the profit and the balance sheet total.

In December 2011 the Company incurred an expense of PLN 15 000 arising out of an invoice for offers posted on an internet portal. The invoice did not specify the relevant period. The company could publish its offers over three consecutive months: December, January and February. However the information about the service provision period could be inferred from an earlier offer. The Company recognized PLN 5000 as the current period's costs, while PLN 10 000 as the next period's costs. However since the document itself did not show the relevant period of time, when the "subscription was purchased", the company might have attempted to recognize the expense (PLN 15 000) as 2011 costs. This would result in the following: a decrease in prepayments (assets), an increase in profit and the balance sheet total.

Similarly, a difficult aspect could be the issue of recognition of the time of qualification of the Company's revenue. IT services could be accounted for as a one off service, they could last several days or several months in some cases. In December 2011 the company issued an invoice for PLN 29 600 (net). The services relating to the invoice in question were performed in December as well as in January, hence the company recognized half of the revenue as the current period's revenue and the other half as the next period's revenue (2012). If the financial department was not aware that a part of the service was performed in January of the following year, the situation might have been different – i.e. the entire invoice could be recognized as 2011 revenue.

The Company guaranteed a PLN 120 000.00 credit facility for one of its customers. The customer's condition significantly deteriorated in the last year analyzed. If the Company found and proved that the probability of a possible repayment of the credit facility was greater than the probability of repayment by the customer, it would have sufficient grounds to recognize a provision for expected losses arising out of the credit facility guarantee. The recognition of the provision would increase the period's financial costs and decrease the company's profit.

Due to the nature of the company's business, accounting policy regarding research and development works could prove to be a rather complex issue. The expenses of PLN 16 000 relating to work on a new program (an application) were recognized as the current period's costs. However, assuming that the company could substantiate that the works could bring about development of a new product model and generate sales in the future, the company could activate the expenses and account for hem over time. As a result, the company's balance sheet intangibles would increase, the operating costs would increase, thus resulting in increased profit and the balance sheet total.

The above described situations and actions could take place in the event change in estimates and accounting policy. Such changes would affect the ultimate outlook of the financial statements. Their legitimacy would be underlined by evidence and documentation affecting the probability of their questioning by a statutory auditor.

The following part of this paper provides an analysis of two particular cases. The main assumptions of the analysis conducted are as following: the entity applies changes in the area of its accounting policies - uses above presented techniques – in order to obtain planned final effects: an increase (case A) and the decrease of total profits (case B). In each of the two cases the possible techniques affecting the financial statement of the entity in order to obtain the particular purpose were selected. Therewith the influence of the selected techniques on the final shape of the financial statement was indicated. The situations analyzed below are fictitious cases which are an attempt to portray two possible models, in which the accounting policy was applied as a tool to influence the financial statements' reported figures.

Case A

The main assumption of the first case is that the Company aims to increase the profits of the reporting period. That is caused by the pressure of CEO who is remunerated in line with the results of the company – directly in the form of bonus depending on the generated profits. It is assumed that the CEO's bonus is 5% of the gross profits of the entity. Under the unchanged conditions the bonus would be PLN 39 434,43. From among previously described creative accounting techniques the baseline techniques which affect the growth of the profits were selected and tabulated below.

Table 5. The selected changes in the accounting policies methods for the case A

No.	Activity	Impact on the profits (PLN)
1.	Resignation of the recognition of the provision for the Management Board' bonus	+ 129 396
2.	Decrease of the intangibles depreciation write-downs	+ 5 000
3.	Decrease of the short-term receivables revaluation write-downs	+ 5 300
4.	Classification of the invoice for the renovation as for the modernization	+ 15 500
5.	Decrease of the long-term investments revaluation write-downs	+ 10 000
6.	Recognition of the next period's revenues as the revenues of the current reporting period	+ 14 800
7.	Accounting policy regarding research and development works	+ 16 000
Total:		PLN 195 996

If the ABC Company made changes in the assumptions and methods of the adopted accounting policies in accordance with the above examples the profits would increase by PLN 195 966. The CEO's bonus would oscillate at the level of PLN 49 234, which would be an increase by about 25% compared to the baseline. In order to assess how the accounting policies changes influenced the whole financial statement of the entity key financial ratios were calculated based on the original values (before changes) and after the adopted amendments. The results are tabulated below.

Table 6. Key financial ratios for the case A

Ratios	Before the changes	After the changes
Liquidity ratio I	4,02	5,64
Return on assets (ROA)	21,07%	25,95%
Return on equity (ROE)	27,00%	33,71%

The introduction of the proposed changes cause the increase of liquidity ratios, return on assets and equity. Thus in general the proposed changes connected with accounting policies affect the growth of the total profits and improvement of the economic and financial condition of the entity assessed on the basis of ratios analysis.

Case B

Case B portrays a reverse situation. It was assumed that the Company aims to decrease the profits in the reporting period what may be caused by the purpose to show growth dynamics in the future. The table below presents selected activities (techniques) that affect the decline of the profits of the reported period.

Table 7. The selected changes in the accounting policies methods for the case B

No.	Activity	Impact on profits (PLN)
1.	Recognition of a provision for the examination by an auditor	-7 000
2.	Recognition of a provision for retirement benefits	-3 600
3.	Recognition of higher depreciation write-downs of the intangibles	-15 000
4.	Increase of the short-term receivables revaluation write-downs	-12 525
5.	Increase of the long-term investments revaluation write-downs	-12 000
6.	Recognition of the next period's costs as the costs of the current reporting period	-10 000
7.	Recognition of a provision for the expected losses arising out of the credit facility guarantee	-120 000
Total:		-180 125

If the ABC Company made changes in the assumptions and methods of the adopted accounting policies in accordance with the above examples the profits would decrease by PLN 180 125. Some of the costs arising from the applied changes that reduce the profits for the year 2011 could be reversed due to some changes in the circumstances in the following year and thus increase the value of generated profits. Such techniques would highlight the dynamic growth of profits in the year 2012. In order to assess the influence of the proposed changes in the context of the economic and financial condition of the Company the key financial ratios were calculated and tabulated below.

Table 8. Key financial ratios for the Case B

Ratios	Before the changes	After the changes
Liquidity ratio I	4,02	3,43
Return on assets (ROA)	21,07%	16,48%
Return on equity (ROE)	27,00%	20,83%

The specified changes would result in the decrease of liquidity ratio, return on assets and return on equity what means the deterioration of the overall financial condition of the Company, which could affect the decisions made on the basis of the financial statement by the stakeholders such as potential investors.

5. SUMMARY

The main purpose of the paper is to stress the importance of accounting policies as an instrument with which business entities create an image of their economic, financial condition as well as other parameters describing the effects of their business activities disclosed in the financial statements. The paper discusses selected theoretical aspects related to accounting policies and on the basis of financial statements of ABC Company it was presented that accounting policies affected financial statements and might be an instrument that created the presentation of financial statements. In the analysed case, a study was performed on the impact of selected assumptions of accounting policies on each part of the financial statements and on the overall presentation of the company's financial condition. Specific examples were quoted to show that modifications of accounting policies and the related estimates may result in an intentional overstatement or understatement of the company's financial result. The analysis was restricted to the impact of accounting policies and modifications thereto on the presentation of financial statements disregarding the aspect of an explicit assessment of the applied techniques in the ethical context.

Accounting policies constitute an inseparable element of each accounting system. Selection of appropriate methods and solutions characteristic for the specific business of an entity within accounting policies is reflected in the presented value of specific items or parts of the financial statements. However, in certain instances, the freedom in selecting methods of accounting policies may be abused by entities and applied in specified purposes. Frequently such abuse of accounting policies occurs during financial crises; even in the opinion of certain authors, such manipulations with financial statements have to a certain extent contributed to generating the global economic crisis. An issue often discussed in that context is the example of selecting a measurement model of elements of financial statements as an element of accounting policies. Critics claim that the application of fair value was a major contributor to starting the financial crisis and adversely affected the financial institutions in the US and all over the world. On the other hand, supporters of fair value accounting argue that it only played the role of a messenger who is shot on the spot (e.g. Turner, 2008, p. 17, Veron, 2008). The analysis of the available results of the study shows that there is no clear evidence that fair value accounting is responsible for the crisis; however, it is not solely a measurement system reporting the value of assets and liabilities without generating economic effects.

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BUSINESS COMBINATIONS

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Abstract: *IFRS standard No 3's objective is to enhance relevance, reliability and comparability of information which an entity provides in its financial statements about a business combination and its effects. Business combinations are accounted for by applying the acquisition method. An acquirer must recognize acquired assets and liabilities assumed at their acquisition-date fair values and disclose relevant information to enable users to evaluate the nature and financial effects of the acquisition. IFRS establishes principles for recognition and measurement of identifiable assets. There are often also newly identified intangible assets acquired. A difference between fair values of net assets and purchase price is a goodwill or a gain from a bargain purchase. There is a number of methodologies how to assess the fair value of assets and liabilities such as income, market and cost approach.*

Keywords: *Business combination, Standard IFRS 3, Valuation methodologies, Fair value of assets and liabilities, Goodwill*

GOALS OF ACCOUNTING HARMONIZATION AND IMPACT OF CULTURAL DIFFERENCES

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Abstract: *In this paper we deal with classification of accounting systems and with effort of accounting harmonization. The main aim of this paper is to discuss the effort of accounting harmonization that started in the last decade of 20th century and highlight the perceived differences between various countries in Europe after two decades. By reviewing recent literature we want to look into possible empirical evidence between the selected European countries. Benchmark of our measurement is the IFRS standards that were being adopted since the beginning of this millennium and officially introduced by EU regulations in 2005 for all companies trading their securities on capital markets.*

We expect to find that even though there is a strong effort to make the rules unique for all European countries the application shows that differences still persist. The differences can be better detected in those countries that started from different accounting background and traditions and also in less prudent countries. This is due to the fact that in particular applications of local GAAPs customs and traditions are impacting on general IFRS rules through their practical application. This phenomenon can be detected through screening of accounting principles and their understanding and practical application in different European countries.

Keywords: *accounting principles, cultural differences, empirical evidence, harmonization, classification*

1. INTRODUCTION

This introductory paper summarizes the goals on accounting **harmonization** on the background of late development at the end of the 20th century and beginning of the new millennium. It attempts to show the major reasons and motivation for accounting harmonisation. The contribution also disuses different classification systems, that were born until these days. Bridging differences in accounting was not an easy task because each national accounting system was established under particular conditions and in specific legal environment. Various classification systems were born in different part of the world.

The need to harmonize the accounting has emerged with the rising business needs to conduct international trade and provide finances to industrial companies and corporations active in other sectors of national economy. The need for harmonization started in the second half of 20th century (Miller, 1990; Emenyonu & Gray, 1992; Hopwood, 1994; Taylor Zarzeski, 1996).

Different reporting standards in individual national states meant that the financial information was not easily understood to international partners, thus the need for harmonisation arose. Further impulse came from financial markets which provide resources to industrial

companies. Here the investors, decision makers and their managers needed to understand the figures – to have comparable information about productivity and attractiveness and future prospect of each individual company to assess their investment alternatives.

The goal was thus established – to harmonize the accounting standards and procedures. But, how to approach it, and where to start?

Companies are coming from different sectors and their reporting needs vary. There is different informational need for public sector companies that get their finances mostly from public sources (taxes) and there are also different requirement for small and medium sized companies, which do not operate on financial markets for the reason of raising money for business and mostly just follow their business life cycle and want to stay in the business serving close community in their surroundings. These companies do not aspire to have any important capital share coming from international trade or financing from international capital markets. So the goals are different.

This leads to the problem of accounting **classification** that tries to capture similarities and differences in different national accounting practices – ways to understanding different accounting systems. Differences in accounting systems arose from legal and cultural back grounds. Cultural background is historically determined by economic, cultural and political evolution of each country.

International accounting standards ought to lead to mitigation of differences. On the other hand it has been observed that IFRS are becoming “nationalized”. After certain time of usage, IFRS become a part of national financial reporting system. They also tend to be influenced by cultural background of each country, accounting “habits”, country tax rule, economic development and particular legal environments. Classification of accounting system is a useful tool to gain broader understanding of possible differences and conflicts in explanation of economic and financial phenomena.

Major factor causing important differences in drawing, interpreting and understanding corporate accounts can be attributed to **cultural differences**. First well known author trying to capture cultural difference in industrial world was Geert Hofstede (*1928) from Tilburg University, Nederland. Professor Hofstede prepared his classification of cultural differences for different purposes, not for understanding and interpretation of accounting but for different interpretation of certain features and managerial instructions in industrial company. His classification was later adopted in different parts of research disciplines and social science works.

As accounting is no different and because its procedures are used internationally, the recognition of cultural differences is relevant. There are various discussions whether Hofstede’s classification is appropriate particularly for accounting, but since there was no other system of recognition of cultural differences at hand, Hofstede’s work became used as important corner stone in understanding international accounting.

In the conclusion of this contribution we try to characterize the **current state of fulfilment** of goals of accounting harmonisation and today’s picture and role of accounting by summing up the review of the influences of different historical backgrounds, cultural differences and different ways of accounting classification.

2. THE NEED FOR HARMONIZATION

National accounting standards typically differ and this results in differences and difficulties in interpretation of financial results of companies. Initially, financial reporting represented mainly internal reporting, and it provided company owners with a vehicle to manage the firm. Later on, in the early 1800s private capital alone was insufficient to finance business activities. Capital started to be gathered from sources outside the company. Furthermore, the owners delegated the managing function to directors and provided them with the necessary authority. Nowadays the external financial report provides a means of conveying the financial results and accounts to owners.

The rationale was, that differences create potential difficulties for users of accounts who need to compare the financial information of companies based in different countries, and for companies which wish to engage in cross-border activities, such as raising finance in more than one country (Thorell, Wittington, 1994; Hopwood, 1994; Miller, 1990; Jindrichovska, 2004, Sucher, Jindrichovska, 2004).

Officially the harmonization of financial accounting was regulated in the EU by two EU directives of the Council of Ministers: the Fourth Directive on the annual accounts of companies (July 1978) and the Seventh Directive on consolidated accounts (June 1983). These have been implemented in the national laws of all EU member countries. By this implementation certain degree of harmonization as has been achieved by the EU.

Accounting academics and professionals perceived problems in harmonization resulting from differences in form and content of accounting statements. There is also great diversity of institutional and legal frameworks – systems based on code law – with closely defined statutory prescription in company law (such as Germany and France) and in contrast systems permitting greater freedom of accounting method.

EU accounting regulations were a part of global system of harmonization of economic institutions – which concerned mainly financial market institutions and rules and regulation of their operating. The main idea of harmonisation was to institutionalize a system of mutual recognition of standards and values. The concept of recognition by stock exchanges is an important force for harmonization not only within the EU but also within the wider world context. However, there were also voices that full recognition might not always be appropriate when the requirements of countries are not, in fact, equivalent. It is also necessary to give room for diversification and innovations. “If international diversity and innovation are to be maintained, the international arrangements for standard-setting must allow and even encourage innovation, provided that it represents an elaboration of the minimum standard of disclosure required by IASC or EU standards.” (Thorell, Wittington, 1994, p. 230)

Firstly, the system of standards and standardized accounts was utilized in large companies, who had similar goals on capital markets. Therefore the standards required by the Fourth EU Directive achieved the minimum degree of regulation of accounting, which has been more effective in the areas of format and disclosure and less so in the case of measurement ¹ Because of complications of reporting in smaller companies the Seventh directive offered exemptions for small and medium companies in the area of drawing consolidated accounts.

The major driving ideas and motivations behind the accounting harmonization can be briefly summarized as follows:

(1) *No country has a completely satisfactory system of national accounting standards.*

There are issues of coverage and compliance

(2) *Accounting standards and practices differ between countries and there are often good reasons for this.*

Reasons may come from history or from institutional settings or from business users of accounts.

(3) *Accounting needs vary with the size and form of corporate enterprise.*

These differences are recognized in domestic legislation and accounting standards. This principle has been adopted by the EC Accounting Directives and there are less demanding reporting rules for SMEs.

Summarized according to (Thorell, Wittington, 1994)

¹ <http://www.sec.gov/rules/concept/34-42430.htm>

Nevertheless, the objective of the EU is to develop a common market, where there is free flow of capital, goods and labour across national borders without institutional obstacles. This is a condition implying harmonization of accounting standards and procedures for all countries and companies. Thus there is a need for accounting harmonisation.

3. CLASSIFICATION

Development of accounting systems in the individual framework of national economic systems is the main reason that differ from one another. The process of harmonization of accounting as a result of the growing needs of comparability of financial data (in the 70s min. Century) created the need for comparable and reliable accounting data and thus identify what the national accounting systems differ. Based on these findings it was possible to proceed with the formation of uniform, generally accepted accounting standards.

Accounting systems as an integral part of national economic environment and they differ in many aspects. Their combination gains a unique form in every national system. Some elements appear in multiple accounting systems and some are individual. Description and classification of accounting systems were one of initial stages of development of accounting standards IAS. Such in debt examination and explanation provides a better description and analysis, based on the classification one can better predict the properties of elements, which arise and are waiting to be discovered (Zarova, 2006).

Determination of four measurable dimensions that differentiate cultures was crucial for the more developed classification of accounting systems. This was elaborated in 1980 by G. Hofstede in his work *Culture's consequences – international differences in work-related values*. The data upon which these dimensions were initially developed came from survey results collected within one large multinational business organization (IBM) in 72 countries. Subsequent surveys had broader base (Hofstede, Hofstede and Minkov, 2010).

The original four dimensions were:

1. **Individualism versus Collectivism (IDV)** – The fundamental issue addressed by this dimension is the degree of interdependence a society maintains among its members. It has to do with whether people's selfimage is defined in terms of 'I' or 'We.' In individualist societies, people are supposed to look after themselves and their direct family only. In collectivist societies, people belong to 'in groups' that care for them in exchange for loyalty.
2. **Power Distance (PDI)** – This dimension deals with the fact that all individuals in societies are not equal. It expresses the attitude of the culture towards these inequalities among us. Power Distance is defined as the extent to which the less powerful members of institutions and organizations within a country expect and accept that power is distributed unequally.
3. **Masculinity versus Femininity (MAS)** – A high or masculine score on this dimension indicates that a society is driven by competition, achievement and success, with success being defined by the winner/best in field – a value system that starts in school and continues throughout organizational behavior. A feminine score on this dimension indicates that the dominant values in society are caring for others and quality of life. A feminine society is one in which quality of life is the sign of success. Standing out from the crowd is not admirable. The fundamental issue here is what motivates people - wanting to be the best (masculine) or liking what you do (feminine).
4. **Uncertainty Avoidance (UAI)** – This dimension deals with the way a society considers the fact that the future can never be known, i.e., should we try to control it or just let it happen? This ambiguity brings with it anxiety, and different cultures have developed ways to deal with this anxiety. The extent to which the members of a culture feel threatened by ambiguous/unknown situations and have created beliefs and institutions that avoid these is reflected in the UAI score (Hofstede *et al*, 2010).

Subsequently, two additional cultural dimensions were established by Hofstede and his colleagues (Hofstede, Hofstede and Minkov, 2010).

5. Long-Term Orientation versus Short-Term Orientation (LTO) – The Long-Term Orientation dimension is closely related to the teachings of Confucius and can be interpreted as dealing with society’s search for virtue; i.e. the extent to which a society shows a pragmatic future-oriented perspective rather than a conventional historical short-term point of view.

6. Indulgence versus Restraint (IVR) The Indulgence versus Restraint dimension consists of two poles. Indulgence stands for an inclination to allow relatively free gratification of basic and natural human desires related to enjoying life and having fun. Restraint, the opposite pole, reflects a conviction that such gratification needs to be curbed and regulated by strict norms.

Gray based on the original four Hofstede cultural dimensions constructed a set of four accounting value dimensions (Gray 1988). that are:

1. Professionalism versus Statutory Control refers to professional judgment and self-regulation in contrast to compliance with rigid legal requirements and legislative control.
2. Uniformity versus Flexibility indicates the level of enforcement of standardized and consistent accounting practices.
3. Conservatism versus Optimism indicates a vigilant approach to accounting measurement, as opposed to a more optimistic and risk-taking approach.
4. Secrecy versus transparency refers to confidentiality and the constraint of disclosure of information, as opposed to a more transparent and publicly accountable approach.

The relationships between the four accounting value dimension and the Hofstede four cultural dimensions are shown in Table 1 and defined in the four hypotheses proposed by Gray (1988).

6. Gray’s Four Hypotheses:

H1 The higher a country ranks in terms of individualism and the lower it ranks in terms of uncertainty avoidance and power distance then the more likely it is to rank highly in terms of professionalism.

H2 The higher a country ranks in terms of uncertainty avoidance and power distance and the lower it ranks in terms of individualism then the more likely it is to rank highly in terms of uniformity.

H3 The higher a country ranks in terms of uncertainty avoidance and the lower it ranks in terms of individualism and masculinity then the more likely it is to rank highly in terms of conservatism.

H4 The higher a country ranks in terms of uncertainty avoidance and power distance and the lower it ranks in terms of individualism and masculinity then the more likely it is to rank highly in terms of secrecy.

Prior to Gray’s study, no research focused explicitly on the relationship between culture and accounting systems and practices had been carried. Prior research on international accounting differences considered the effects of a broad range of environmental factors on the development of accounting systems and on structural patterns that could be used to classify the different accounting systems (Mueller, 1967; Zeff, 1971; Radebaugh, 1975; Nair & Frank, 1980; Nobes, 1983a, b). The nature of these studies is discussed extensively in Gray’s classical work (Gray, 1988).

Accounting research is one of numerous disciplines which utilize Hofstede’s classification and quantification of cultural differences. Some authors have questioned and are still questioning the validity of the scientific rigor of this concept classification. For example Baskerville points out that there is “the lack of a robust theoretical basis for research using Hofstede’s indices”. Baskerville identifies “problems especially in the following aspects: a) the assumption of equating nation with culture, b) the difficulties of, and limitations on, a quantification of culture represented by cultural dimensions and matrices; c) the status of the observer outside the culture”. The author

points out possible risks of mortification of cultures in several parameters, and in its use as explanatory variables accounting for the differences between approaches in different countries: “the manner in which Hofstede established the dimensions of culture, and the subsequent reification of “culture” as a variable in cross-national studies in accounting research, led to a misleading dependence on cultural indices as an explanatory variable of differences in accounting practices and behaviour” (Baskerville, 2003). In another context the author supposes, that management disciplines are in more “danger” than accounting from the expansion of this methodological approach. McSweeney (2002) claims that crucial assumptions which underlie Hofstede’s assertion to have uncovered the secrets of entire national cultures are unreliable and challenged Hofstede’s model of national cultural differences and their impact.

The definition of “cultural differences” by G. Hofstede undoubtedly provided an effective tool for identifying and measuring differences between national environments in the area of financial reporting. Comparative accounting research has provided an enhanced awareness of the influence of environmental factors on accounting development. This research has contributed to a growing realization that fundamentally different accounting patterns exist as a result of environmental differences and that international classification differences may have significant implications for international harmonization and the promotion of economic integration.

On the basis of set parameters several national accounting systems have been divided into groups. Nair and Frank (1980). distinguished five models²:

- 1) UK: Great Britain, Australia, Ireland, Netherlands, New Zealand, South Africa, Bahamas, Jamaica, Iran, and others,
- 2) Latin American and southern Europe: Brazil, Peru, Uruguay, Panama, Argentina, Bolivia, Greece, Italy, Pakistan, Colombia, and others,
- 3) North and Central Europe: Austria, Belgium, Denmark, France, Germany, Norway, Sweden, Switzerland, and others,
- 4) Spheres of influence of the U.S.: the U.S., Canada, Japan, Mexico, and others,
- 5) Separate group: Chile.

Table 1. Ten groups of accounting systems were distinguished based on Gray’s accounting value dimensions (Gray, 1988)

Group	Country
Anglo-Saxon	United Kingdom, Ireland, USA, Canada, Australia, N. Zealand, South Africa
Germanic	Germany, Austria, Switzerland, Israel
Nordic	Denmark, Finland, Sweden, Norway, Netherlands
Developed Latin	France, Belgium, Italy, Spain, Brazil, Argentina
Developing Latin	Portugal, Mexico, Costa Rica, Guatemala, El Salvador, Panama, Venezuela, Colombia, Peru, Ecuador, Uruguay, Chile
The Middle East	Arab states, Turkey, the former Yugoslavia, Greece
Developed Asian	Japan
Developing Asian	Indonesia, Pakistan, Taiwan, Thailand, India, Malaysia, Philippines
Colonial Asian	Hong Kong, Singapore
African	countries of East Africa, West Africa

In the next studies and analyses of accounting system more differences were identified using more classification parametres on the other hand the analysis confirm only a few of the most significant differences. More precisely only two essential differences: “All of Anglo-American countries are societies with strong democratic values and a long standing tradition of publically traded stock companies. All these countries support financial reporting that emphasizes the information needs

² Note: Classification did not include accountin systems of centrally planned economies in the CEE.

of equity and other investors in the capital markets. This is in sharp contrast to countries where financing has traditionally been associated with large banks or state funding. The accounting standard setting boards in the Anglo-American countries are generally independent organizations of professional accountants and even in Australia, where the Australian Accounting Standards Board (AASB) is part of the national government, there is broad acceptance of the public accountant's independence of judgment on professional matters." (Borker, 2013).

The great influences were also identified in the type of legal system, i.e. code law and the common law: in Code-law countries stakeholder governance rests in a few hands (i.e. the government or lending institutions), in Common-law countries the stakeholder governance is more diverse and dispersed, greater significance has an accountant profession.

This became the base of differentiation of four models. The former classification was aggregated in three models: the Anglo-Saxon, Continental, and South American and supplemented by a new group of accounting systems made up the "*mixed model*". This is the label for accounting systems in member countries of the former Soviet Union and Eastern and Central Europe. These accounting systems were not analysed in more detailed characteristics to be included into the previous classification. Reconstruction of the accounting system in these countries is a part of the transformation from centrally controlled states to a market based economies. This transformation also changes the shape and purpose of the present accounting systems, which is from its beginning under the growing influence of international accounting harmonization *cf.* Nobes 1983a and Nobes 1983b.

More than thirty years have passed since the first attempt of identification of the differences of accounting systems was attempted. In this period the system of IFRS, which is in place since 2005, became a part of the national accounting system. The adoption of IFRS for the preparation of financial statements is mandatory for the listed companies and became a part of the national accounting system of many countries. In most of the European countries where the accounting system is closely linked to the tax system are company financial statements prepared in both the national and the IFRS formats. The accounting system has gone through many changes on both the international level and in the local national context. Also, the information needs of the users are closely linked with the development of the world and national economy. At the same time, the global influence is increasing.

Even at this stage of development the classification of accounting systems does not lose its importance. The reasons of its importance have been highlighted by Nobes (2008).

- a) The degree and extent to which national regulators allow the use of IFRS differs,
- b) In many countries that have adopted IFRS for the consolidated statements of listed companies, a large part of the accounting system is under the influence of international accounting standards, which remains the reason for the classification,
- c) The degree to which national accounting system converge with IFRS (adopts IFRS) are different, which is the reason for the classification
- d) The fact that foreign accounting systems (accounting standards) are recognized by the national stock exchanges is the reason for the accounting classification.
- e) IFRS implementation process is carried out through preparation of national versions of IFRS (IFRS are adapted to local conditions), which is the reason for the classification.

Nobes also worked out a new classification system according to degree of implementation of IFRS in national accounting systems:

A) countries where the national standards are required for the unconsolidated statement (for tax purposes) – Austria, Belgium, Czech Republic, Germany, France, Hungary, Latvia, Lithuania, Poland, Portugal, Slovakia, Spain, Sweden, Switzerland.

B) countries where the national standards are not required for the unconsolidated companies – Cyprus, Denmark, Estonia, Ireland, Italy, Luxembourg, Malta, Netherlands, Norway, Slovenia, UK (Nobes, 2006).

Together with a process of implementation of IFRS into national accounting environment is reflected also in other parameters reflected in the results of the use of IFRS for financial reporting. These parameters affect the way, how are the general accounting principles and procedures implemented. And also how do they affect the selection of particular accounting procedures in the case that several options are available and therefore how they affect the overall explanatory power of corporate financial reports. In this way IFRS adopt the local characteristics of particular national environment. It turns out that these parameters show the cultural characteristics of the country throughout the whole summary of accounting concepts and in more detailed structure. And furthermore, their differentiation finds its basis in Hofstede's classification of cultural differences.

These features were also pointed out by Albu and Alexander (2012) "...due to various factors (culture, lack of detailed rules etc.), the application of IFRSs is not uniform and the issue of de facto convergence emerges. ...".

Another level of conflict between the application of new requirements and the spirit of IFRS, appears in daily practice of accountants – the excessive rules-based approach of practical accountants. (In the case of SMEs the accountants become merely "bookkeepers" rather than true "accountants"). The lack of professional judgment and the *de facto* fiscal influence seem to be the most threatening factors for accounting profession.

The process of implementation of IFRS in national accounting systems around the world attracts the attention of researchers, which devote particular attention to the cultural differences in these new internationalized conditions. The new quickly developing countries, such as India, China and South-east Asia, have either implemented the IFRS in their original form (India) or in the form adjusted for the national conditions (China). This process creates opportunities for new research and implies new dimension of cultural differences.

For the above listed countries it transpires that: "...the existing models that cluster countries are substantially incomplete and misleading due to the recent convergence efforts that have taken place. We identify the factors that may be causing differences in both the *de jure* and *de facto* aspects of comparability in financial reporting across countries in the post-convergence period,... there are three dominant factors that still act as constraints in accounting convergence: (1) the nature of business ownership and the financial system, (2) culture, and (3) the level of accounting education and the experience of professional accountants in each of the different countries." (Chand *et al*, 2008)

Another very significant reason of cultural differences stems from the way of thinking – which is a special part of the cultural features: "*Eastern Asians tend to think holistically and pay more attention to the context and relationships among the elements in the context. But Western people tend to think analytically and pay more attention to dispositions. Therefore, different ways of thinking may influence how individuals process the information...*" „*When Eastern Asians read analytic ads, their holistic way of thinking will be activated. As a result, Eastern Asians will engage in greater cognitive elaboration and consider and generate more thoughts not provided in analytic ads. Eastern Asians will develop less favorable attitudes toward analytic ads because such ads are not congruent with their cultural orientation* (Beichen Liang, 2007).

As to the issue of the special condition in emerging economies and specific features and factors influencing the implementation of IFRS the authors emphasize, that understanding *how* IFRSs work in relation with local actors/institutions is very important and "little is known about the means (institutions, organizations) through which these global (western) standards are "imported" and how "the translation and customization" is realized (Albu and Alexander, 2012; Ezzamel and Xiao, 2011).

4. CULTURAL DIFFERENCES – REVIEW OF EMPIRICAL EVIDENCE

With the beginning of 2005, the EU began requiring consolidated financial reports of publicly traded firms to be prepared in accordance with the EU-endorsed International Financial Reporting Standards (IFRS) in an effort to increase the comparability of financial information across EU Member States. While some experts agree, that IFRS reporting helps to increase the comparability of financial information across the EU, others argue that comparability is unlikely because IFRS implementation will vary according to national institutions and culture (Liao, Sellhorn, Skaife, 2011). Tsakumis, Campbell and Douppnik (2009) pointed out that recent accounting research suggests that among countries that have adopted the same version of IFRS two factors – national culture and language translation – could undermine the rigorous interpretation and application of IFRS and lead to a lack of comparability across countries. Their research suggests that cultural differences cause accountants in different countries to interpret and apply accounting standards differently. This research reveals that two accounting values that are directly influenced by national culture are conservatism and secrecy, which affect the measurement and disclosure of financial information in financial reports and have the greatest potential to affect cross-border financial statement comparability. The underlying framework helping to explain these findings is based upon one of the largest cross-cultural surveys ever conducted by Geert Hofstede.

National culture is most likely to influence the application of financial reporting standards where judgment is required. This is of concern since most of IFRS is principles-based. This requires substantial judgment on the part of the accountant. Recent research has found that national culture influences both the interpretation and application of accounting standards across countries.

The results of Liao *et al* (2011) indicate that French and German IFRS earnings and book values are comparable in the year subsequent to IFRS adoption, but become less comparable in the following years. They document differences in accounting estimates, recognition of special items, and other equity reserves between French and German firms, which help explain the decrease in comparability over time.

Their study focuses on France and Germany because these two countries represent the EU's major economies and largest capital markets denominated in the Euro, suggesting these two countries have equally efficient equity markets. Moreover, France and Germany have some similar social-economic institutions that prior research indicates affect firms' accounting measures (Alford *et al*, 1993; Gernon and Wallace, 1995; Ball *et al*, 2000; Bushman and Smith, 2001; Brown and Tarca, 2007). At the same time there exist institutional differences between France and Germany that can influence managers' accounting implementation choices and can affect the comparability of financial information. (Stulz and Williamson 2003; Nobes and Schwencke, 2006; Enriques and Volpin, 2007)

According Ramanna and Sletten (2009) the countries do not adopt IFRS all at once, but they prefer individual understanding in across countries. They focus their analysis on a sample of 102 non-EU countries and examine IFRS adoption over the period 2002 through 2007 and network effects at the regional and trade levels. Accordingly, they test whether the likelihood of IFRS adoption for a given country in a given year increases with the number of IFRS adopters in its geographical region and with IFRS adoption among its trade partners.

Economic network theory predicts that in addition to network benefits such as synchronization value, a product with network effects can be adopted due to its direct benefits (Katz and Shapiro, 1985; Liebowitz and Margolis, 1994). In the case of the IFRS adoption decision by certain country, they argue, that direct benefits are represented by both the net economic and net political value of IFRS over local standards. The net political value of IFRS is the benefit arising from the potential political nature of international accounting standard setting.

If countries expect the EU to have a dominant role in IASB affairs (Brackney and Witmer, 2005), they are likely to have to give up some authority over standard setting to EU interests. Submission of authority over local standards is, in turn, likely to be less convenient to more

powerful countries, which leads to the prediction that more powerful countries are less likely to accept IFRS.

Ramanna, Sletten (2013) described, that the International Accounting Standards Board (IASB) was established in 2001 to develop International Financial Reporting Standards (IFRS). In the period from 2003 through 2008, more than 50 countries (including the EU countries) mandated IFRS for all listed companies in their jurisdictions. Further, in that period, another 15 countries either mandated IFRS for some listed companies or allowed listed companies to voluntarily adopt IFRS. Another group of 15 countries initiated “convergence” projects with IFRS through 2008, and the list of states with convergence projects extending beyond 2008 includes some of the world’s largest economies such as China and the U.S.

There has been considerable research into the consequences of a country’s IFRS adoption for firms in its jurisdiction (e.g., Armstrong et al 2010; Daske et al, 2008; DeFond et al, 2011, and Lang *et al*, 2010); but less is known is the motivation **why** countries themselves adopt IFRS. The notable exception is Hope, Jin, and Kang (2006) who find that disclosure practices, investor protection, accessibility of equity markets to firms, and the size of equity markets are linked to countries’ adoption decisions.

They complement this research by developing and testing the hypothesis that the inter-temporal shift towards IFRS over local standards can also be explained by perceived network benefits, i.e., perceived lower transactions costs, given the network of IFRS adopters. If true, the implication is that worldwide IFRS acceptance is self-reinforcing, i.e., adoption inspires and causes further adoption.

The following diagrams depict matrices of examination items for IFRS. In an IFRS adoption project, account processing policies, operation, IT and organization are the main items for consideration.

Figure 1 Scope of impact, major processes and implementation approach

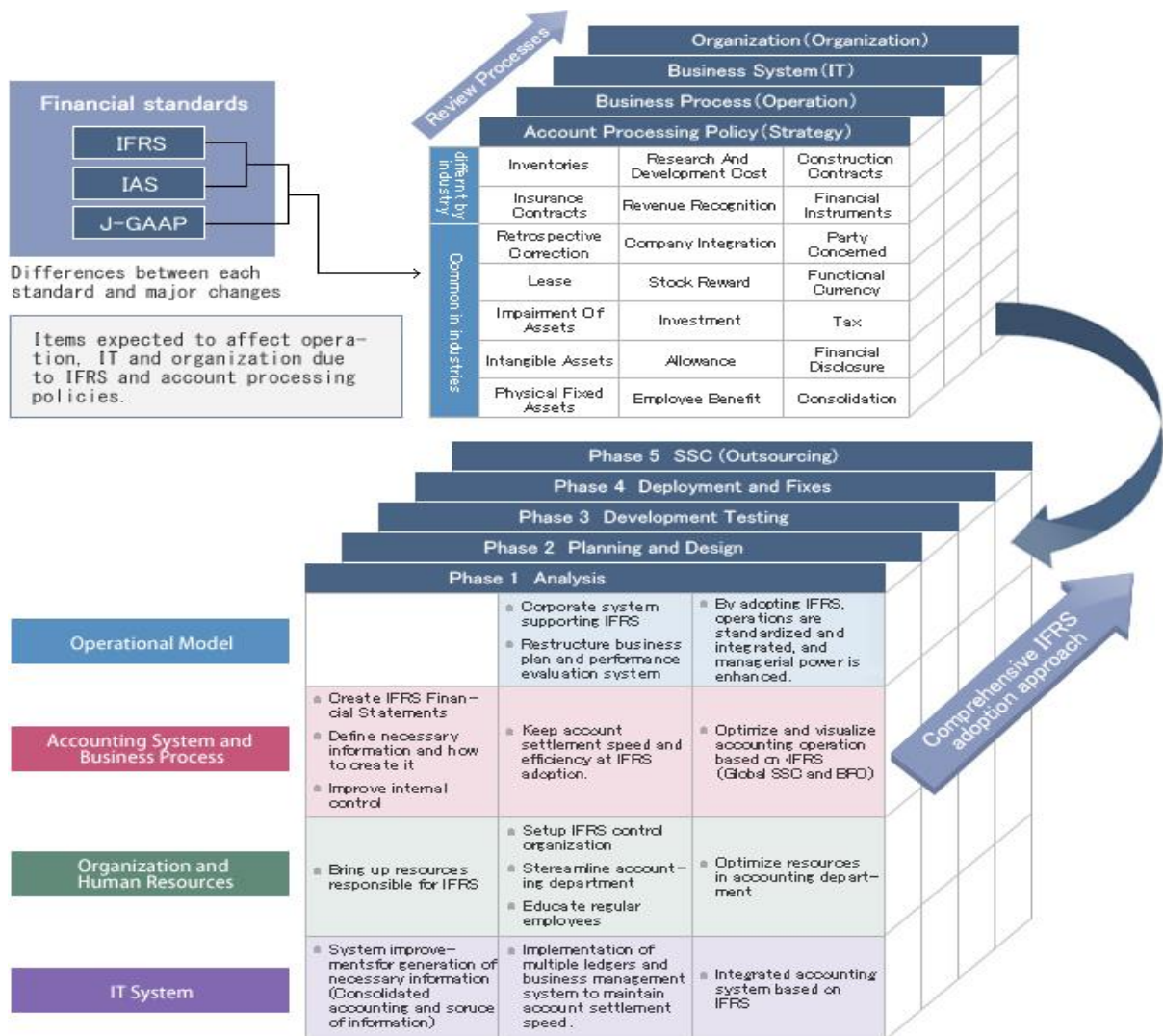


Figure 1. Scope of impact, major processes and implementation approach

Source: Pacific Business Consulting. IFRS consultation services. [on-line 190913]

<http://www.pbc.co.jp/en/service/ifrs.html>

Ramanna, Sletten (2013) founded, that the presence of network effects in the adoption of IFRS is significant because it means a country can adopt IFRS even if its domestically developed accounting standards are particularly well-suited to its domestic institutions. Moreover, if network effects contribute to the adoption of IFRS, they can sustain its eventual dominance even in the presence of technologically superior innovations (David, 1985). The evidence in this paper can also complement the growing literature on the determinants and consequences of firms' IFRS adoption. Firms' adoption decisions are conditional on countries' decisions to harmonize with IFRS, suggesting that the analysis of why countries adopt IFRS is important. The growing literature on the consequence of IFRS adoption to firms can, in turn, inform studies that analyse country-level decisions; governments are likely to consider expected firm-level consequences when choosing to allow or require IFRS.

The concept of network effects has recently been used to explain several accounting related phenomena, such as the adoption of stock-option compensation plans and decision to expense options in the income statement (Reppenhagen 2010). We document that network effects influence accounting-related decisions more generally, suggesting network theory can be used broadly in the literature on accounting and corporate governance choice. For example, the theory of IFRS

network benefits tested herein in the context of countries can equivalently be applied to firms. Future firm-level research can investigate whether network benefits increase the attractiveness of voluntary IFRS adoptions to multinational as opposed to domestic corporations.

Ding, Hope, Jeanjean, Stolowy (2006) summarized the information on accounting practices in 15 countries (European countries, the U.S., Canada, Australia and Japan) plus IAS. Ordelheide and Semler (1995) proposed the TRANSACC Reference Matrix. They provide a comprehensive examination of different accounting methods. However, their analysis is restricted to the most developed countries in the world. Several subsequent studies have used this matrix to classify countries according to their accounting differences (e.g. d'Arcy, 2001).

Ashbaugh and Pincus (2001) seek to determine whether the variation in accounting standards across national boundaries relative to IAS has an impact on financial analysts' ability to forecast non-U.S. firms' earnings accurately. They analyze accounting practices in 13 countries to identify differences in countries' accounting standards relative to IAS, covering both differences in disclosure requirements and measurement methods for IAS versus sample firms' domestic GAAP in 1993. Besides Ashbaugh and Pincus (2001), few extant studies examine the comprehensiveness of a given set of accounting standards in comparison with others³. There is thus ample room for improvement in the existing measurements for international accounting differences.

Ding, Hope, Jeanjean, Stolowy (2006) examined differences between local GAAP and IAS. IAS is a logical benchmark to use due to its growing importance worldwide. Similar to U.S. GAAP, the IAS framework has an investor focus (where "investor" is defined broadly), and consequently **these** measures – absence and divergence – should be interpreted with this in mind. One of the contributions of this study is that they construct a measure of differences between national GAAP and IAS based on the survey "GAAP 2001: A Survey of National Accounting Rules Benchmarked against International Accounting Standards." This survey was published jointly by seven large audit firms: Andersen, BDO, Deloitte Touch Tohmatsu, Ernst & Young, Grant Thornton, KPMG and PricewaterhouseCoopers. In this survey, partners in the large audit firms in 62 countries were asked to benchmark their local written requirements against some 80 accounting measures, focusing on both national and international standards in force for the financial reporting period ending 2001 (Nobes, 2001).⁴

Study of Ding, Hope, Jeanjean, Stolowy (2006) provides empirical evidence of links between financial reporting standards and the economic, financial, and governance institutions in a country. An important contribution of this study is that we construct interesting measures of international accounting differences which have not been used in prior literature. These measures are two-dimensional – absence and divergence. Specific rules on recognition, measurement and disclosure may be absent in domestic accounting standards (DAS) compared with IAS.

Divergence represents inconsistencies in national accounting rules regarding certain accounting issues with those of IAS. They show that the level of absence is higher in countries with less developed equity market and with a higher ownership concentration. Divergence between DAS and IAS is positively associated with the economic development and the strength of the accounting profession but is constrained by the importance of equity markets. These results corroborate and complement those of extant research (e.g., Ball *et al*, 2003; Hope, 2003a) and have important implications for the harmonization of the accounting standards. That is, accounting institutions do not exist in isolation but in a mosaic of complex sets of institutions. Merely changing one link (i.e., accounting standards) may not be sufficient to substantially improve the financial reporting quality unless changes to the capital market development and legal environment are brought about simultaneously. This raises an important issue: although the application of IAS

³ Bushman, Piotroski, and Smith (2004) examine links between corporate transparency and several corporate governance variables using an international sample.

⁴ Street (2002) provides a summary of the GAAP 2001 survey.

is meant to achieve uniformity worldwide, it is possible that this desired uniformity may remain elusive due to the lack of simultaneous changes in other accompanying institutions.

Zori (2013) pursued different or similar will the outcomes (results) of IFRSs application(s) be if some countries adopt IFRSs without modifications as compared to those that apply modified versions of the standards.

Generally, IFRS adoption is the responsibility of a particular institution. Although these institutions and their mandates may differ from country to country, the pronouncements on the adoption of the standards may look similar. On a broader scale, announcements on IFRS adoption may take the following wording

Important phrases used in IFRS adoption pronouncements

The country/company has adopted...

1. IFRS as issued by the International Accounting Standards Board
2. IFRS as endorsed by the European Union
3. IFRS as adopted by the accounting regulator
4. IFRS as permitted by the accounting regulator

This range of terms in itself demonstrates the bandwidth of possibilities within “adoption” of IFRS.

Accounting regulators often have the authority to make pronouncements on the adoption of IFRS. This authority possessed by the accounting regulator is usually driven from the constitution via the issuance of an act or certain by-laws. To obtain the version of IFRS adopted in a country, it is therefore important to review the pronouncement of the accounting regulator or the institution with the legal authority to make such pronouncement. In this pronouncement, there is also the need to examine the statement of pronouncements by looking at the key words used to ascertain the version of IFRS so adopted in the country.

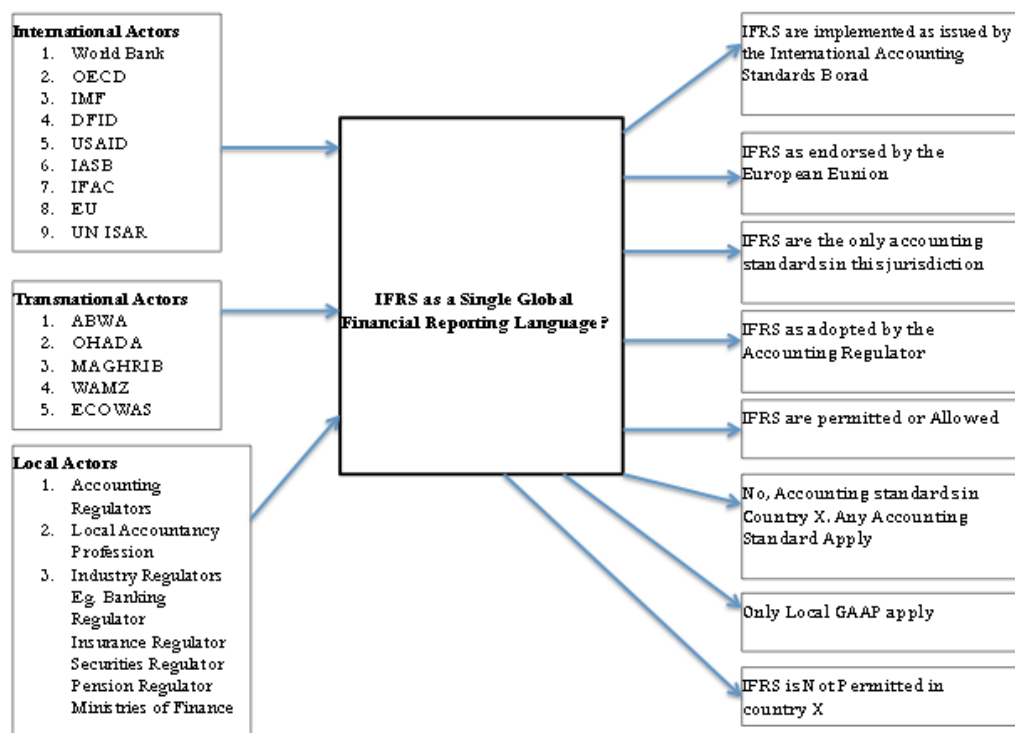


Figure 2. Wide Variations in IFRS Adoption
Source: Zori (2013)

Meanwhile, divergence of DAS from IAS is associated with low synchronicity but is not significantly related to earnings management. This finding corresponds to the first possible interpretation of their final hypothesis; divergence from IAS could mean standards that are better tailored to the needs of local legal and business environments. A limitation of this study is that, given these relatively small sample of country-level observations, they are not able to jointly consider the determinants of and economic consequences of differences in financial accounting standards. Such a test would have the potential to strengthen this inferences regarding whether the results we observe for earnings management and synchronicity are in fact due to the hypothesized effects, or whether they are affected by factors that help explain variation in accounting standards in the first place.

Baskerville, Evans (2011) provided analysis of five issues faced by translators, drawing examples from each of the major language family groups in the EU. The data used in this study are derived from 109 responses to a survey of IFRS translators, members of IFRS. Each Language Family Example' illustrates deeply-held convictions about language; and diversity of views even among highly experienced translators. These empirical data also illustrate translators 'awareness that the English 'in which IFRS are written may impact on the ease or difficulties in translation. In nation-states where there is a relatively low level of foreign language study, there may be a greater number of accounting teachers, standard-setters, textbook writers and regulators who are unaware of such diversity and emotion.

According to their results they recommend the use of a version of the English language in standard setting tightly maintained and consistent within all IFRS. Not only translators, but a diverse set of user groups including many English-speaking educators and students of the profession need standards which they are written in consistent, concise and clear English. At present, many are not. The success, or not, in recognition of this issue has implications for the overall success of the convergence project for the US and IASB/IFRS: Less is better, and the means of achieving this is retention of principles-based rather than rules-based standards.

Paul (2007) examined the impact of globalization on international accounting harmonization. The business community has admitted that the accounting is "the language of business". They are using the accounting to communicate the existence and the evolution of the financial situation and also of the performance for the economical entities. Financial information is a form of a language. And if the language of financial information is to be put to use, so that investment and credit decisions can more readily be taken, it should not only be intelligible, it should also be comparable.

The harmonization would be beneficial to those countries, which do not have adequate codified standards of accounting and auditing, and to international accountancy firms with clients of firms, which have at least one foreign subsidiary. Nobes and Parker (2002) because will allowed the comparisons without any other compilations. The benefit of International Accounting firms regarding the harmonization of accounting practices will be the movement of staff across national boundaries will become easier and it will be less expensive to provide training to their staff.

The most fundamental of obstacles to harmonization are (Nobes & Parker 2002):

1. *the size of the present differences between the accounting practices of different countries,*
2. *the lack of strong professional accountancy bodies in some countries, and*
3. *the differences in political and economic systems.*

If accounting measurement rules were the only difference among countries, then straight forward translations would be sufficient to enable reports to be universally understood and interpreted (Mednick 1991). However, countries also exhibit substantial economic and cultural differences that preclude simple interpretations, even when the figures are generated using the same accounting principles. Accounting standards in any society are an outgrowth of that society's needs and perspectives. For example, British and U.S. accounting rules reflect the concepts of

fairness and substance over form as opposed to the French Commercial Code, which is much more compliance-oriented.

Tsalavoutas, Andre, Evans (2012) examined whether accounting quality changes as a result of IFRS implementation in the stakeholder and tax driven accounting environment of Greece, they contribute specifically to the debate on whether shareholder-focused accounting principles are more value relevant than the traditional continental European accounting regulations (e.g. Ball, 2006). This debate reflects on the usefulness of IFRS for investment decisions, given that IFRS consider investors the main users of financial statements. Additionally, by examining the incremental value relevance of the information provided in the reconciliation statements, they explore the usefulness of these mandatory transitional reconciliations as an indication of the market's 'evaluation' of new information. **These** findings are in line with those of Christensen, Lee, and Walker (2009) and Alciatore (1993), who indicate that reconciliation statements do convey useful information to investors.

Perramon, Amat (2006) who deal with impact of publicly traded companies in the European Union which have to comply with the International Financial Reporting Standards (IFRS) for their consolidated accounts, as required by European Commission Regulation. The new accounting rules will facilitate not only the process of international harmonization of financial statements, but also efficient performance of financial markets and capital flows worldwide. Their study analyzes the first results of IFRS implementation by Spanish non-financial listed companies. The results confirm that the introduction of international accounting standards may influence the profit results most likely primarily due to the application of fair-value for derivative instruments and new rules for accounting for goodwill. It seems that the new accounting methods under IFRS, especially for costs capitalization, post-employment benefits and associated companies, introduce material differences in the income statement of Spanish companies. The empirical test reveals that the adoption of IFRS in Spain has a diverse effect on the net profit, which makes it difficult to predict its impact on the other listed Spanish companies. However, the data analysis shows that the difference that IFRS causes for the consolidated profit does not depend on the profit rate and total assets of the companies. This conclusion implies that the adoption of international accounting standards may influence similarly Spanish companies of different size and profitability.

To conclude this part, it has been revealed in empirical studies that transition to IFRS is a reason of many differences in various aspects and levels in the whole system of reporting in national economies. Implementation of IFRS into the national accounting system has changed practices and practical application of accounting standards – the practice how is accounting performed in each particular country, on the other hand, the national accounting system influence application of IFRS.

5. CURRENT STATE OF FULFILMENT

The purpose of the International Financial Reporting Standards (IFRS) is to increase comparability of reporting on financial position and financial effectiveness of different companies, operating under different national conditions. Their roots are in the Anglo-saxon accounting system, grown up from the different social environment, economy development and history in close connection and under the condition of common law. This is the main reason of the differences not only in the specified procedures, but also in the process of the application of accounting procedures in practice. Common conclusions of the studies analysing these differences is that the impact of IFRS implementation across the countries is very much influenced by the previous history, of cultural specifics and local characteristics of economy, that are formed not only by the specific legal environment and tax regulation but also by the customs, common thinking of the accountant profession as well as managers, regulators etc.

According to the international agreements since the year 2005 all the companies operating on the EU capital markets have to prepare the financial statements in accordance with the IFRS. In the same time, however, for the purpose of calculation of their tax liability they are required to prepare the financial statement according the national accounting standards.

To characterize the current state of fulfilment of goals of accounting harmonisation and practical usage of implementation of IFRS we have attempted to analyse the economic motivation of accounting harmonization. We have then characterised the attempts and different approaches to classification of accounting systems. Further we have highlighted the role of cultural difference and their impact on accounting standards and their interpretation in various cultural settings. We have shown how the international accounting standards are interpreted and what are the main features and modifications in various European countries. This leads to various versions of national IFRS. Importance of fulfilment of the Fourth directive is stressed. The Seventh directive is more problematic as it requires harmonization of content.

In our opinion accounting statements will keep to be interpreted differently even though the standards are common. Interpretations are getting closer in general. Different routines will need to be adopted for small and medium enterprises which do not have so extensive reporting needs. Similar situation is with state run enterprises in public sector (schools, hospitals, cultural devices) and other non-profit organizations.

Transition to IFRS is a reason of many differences in various aspects and levels in the whole system of reporting in the national economy system. Their implementation and inclusion into the national accounting system has changed the national systems and, on the other hand, the national accounting systems influence general application of IFRS. We have shown how the international accountings standards are interpreted and what are the main features and modifications in various European countries. This leads to various versions of “national IFRS”.

The intended effects of application of IFRS are accompanied by the unintended secondary effects. The harmonization of the financial reporting is limited by the real reporting limitations in case of the SMEs. This and many other issues inspire the new research that is set up to investigate the accounting practices and habits, its theoretical grounding and limits of practical applications.

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VALUATION OF COMPANIES IN A TRANSITION ECONOMY: COMPARISON OF COMPANIES FROM THE POLISH, GERMAN AND FRENCH MARKETS

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Abstract: *The goal of this paper is to determine to what extent the companies from a transition economy of Poland are valued differently than comparable companies from two continental markets: Germany and France. The novelty of our approach rests in a careful construction of the comparable sample, which is challenge given that Polish companies are relatively small in terms of market capitalization. Therefore we limit our sample to companies for which we can find comparables in the other two markets and then use sample matching techniques to identify the comparables. We study the period after the mandatory adoption of the IFRS and study IFRS reporting companies only. We employ three different accounting-based valuation models with control variables including proxies for accounting quality and find that significant differences in the valuation parameters in fact exist after the adoption of the IFRS: Polish companies are valued higher relative to their accounting performance than the comparable companies from Germany. The findings imply that the quality of national accounting practice is not a concern for international investors who trade in Polish securities.*

Keywords: *panel data, Poland, value relevance*

1. INTRODUCTION

Mandatory adoption of the International Financial Reporting Standards (IFRS) in the European Union was conducted in order to improve the usefulness of financial statements by increasing the comparability of financial statements and their value relevance. Moreover, International Accounting Standards and International Financial Reporting Standards are believed to be standards superior to national accounting regulations (Barth, Landsman, Lang 2008). The mandatory transition to the IFRS became a natural experiment which stimulated research aimed at evaluating the results of IFRS adoption. Since the IFRS were adopted across Europe, comparative studies can include many countries, including transition economies of Central and Eastern Europe.

The goal of this paper is to determine to what extent IFRS reporting companies from a transition economy of Poland are valued differently than comparable companies from two developed continental markets: Germany and France. The study design takes into account structural differences between companies from the three markets which could cause differences in valuation model parameters regardless of the accounting standards used. In order to increase the internal validity of our study, we construct comparable samples by limiting the base sample of Polish companies to those for which we can find comparables and then using sample matching techniques to find comparables from the other two markets.

The contribution of our paper is twofold. First, we contribute a research method which deals with the problem of economic heterogeneity of samples from different national markets.

The use of sample matching techniques allows us to make meaningful comparisons between companies from a transition economy and those from developed economies. Second, we show that after IFRS adoption companies from a transition economy are not valued lower than companies from developed economies. In fact, we find no evidence of significant difference in valuation model parameters between samples of Polish and French companies. The comparison of Polish and German samples shows that German companies are valued lower relative to their profitability than Polish companies. Results suggest that the comparability of IFRS financial statements published by Polish companies is not a concern to international institutional investors who shape stock prices.

The rest of the article comprised of five sections and is organized as follows. In the next section we discuss financial reporting in countries of different institutional settings, focusing on the countries which are included in our study: Poland, Germany and France. In the third section we briefly characterize the accounting harmonization process in Europe including mandatory IFRS adoption. The fourth section is devoted to the presentation of extant international comparative research. In the fifth section we develop the main hypothesis of the article and describe the methodology used in the paper. We present the results in the sixth section and then close the article with conclusions, limitations and further research possibilities based on the contribution of the paper.

2. INTERNATIONAL DIVERSITY OF FINANCIAL REPORTING

The objectives of financial reporting have been historically varied between countries. The main reason for the differences is the balance between various groups of stakeholders which formed in a given country. Generally, empirical research is concerned with two main models of financial reporting, referred to as the Anglo-Saxon model and the continental model. In countries associated with the continental model, banks (or generally financial institutions), tax authorities and other government bodies are the most important groups of users of financial statements. In countries which follow the Anglo-Saxon model, financial reporting has evolved with the assumption that the shareholders are the most important user group and are therefore entitled to receive useful financial information. The scope of this study is set to the continental accounting model: Poland, Germany and France.

The three countries studied here tend to be classified as representatives of the legal compliance or macro-uniform accounting model, a model which tends to exist in countries where corporate ownership is concentrated and therefore the demand for external reporting is limited (Gernon & Meek 2001). In all three countries accounting practice is heavily influenced by a strict, rule-based accounting law and a requirement to use tax accounting methods in the books. Thus, national accounting traditions contrast with the faithful representation model associated with the IFRS. Since the adoption of International Financial Reporting Standards (IFRS) in the European Union financial reporting by stock exchange listed companies has been harmonized in terms of the required elements of financial statements, rules for identification, measurement and presentation of transactions. Comparability was further improved by capital market directives which harmonized rules for interim reporting and statutory audit.

The Polish capital market needed to be created from basics after the fall of communism in 1989. However, the new national accounting law was initially created with the purpose to increase tax revenue and serve the needs of creditors, not investors, which was a response to the concerns associated with the turbulent development of the free market in the initial stage. The Warsaw Stock Exchange began operations in 1991 when 9 companies were listed and it was not until the year 2000 when the number of listed companies exceeded 200, while in 2012 there were 444 companies listed in the main market and a similar number listed in the alternative market called NewConnect. In fact, the number of IPOs in both markets in 2012 exceeded 100, four

times more than at any other continental stock exchange. The dynamic development of the Polish capital market required a rapid pace of regulatory adjustments (Dobija and Klimczak, 2010).

While Poland is gradually converging to the neighbouring countries, Germany and France have been closely related in economic and institutional terms for decades, because the two countries are longstanding members of the European Union. Before the adoption of IFRS, stock listed companies in both Germany and France followed conservative national accounting standards, with strong emphasis on compliance, rather than faithful representation. The local accounting systems had been well developed; hence the introduction of the IFRS was associated with significant changes in accounting methods (Ding et al., 2006). Historically, both systems favoured the information needs of creditors and tax authorities rather than those of the shareholders. In France, accounting is characterized by the use of a standard chart of accounts (Delvaile, et al., 2005). In Germany, financial accounting is influenced by tax law, because only one set of accounting methods is allowed (Roberts et al., 2008). German commercial law entices companies to smooth earnings so that dividend pay-out ratios can be kept at a stable level (Goldberg & Godwin, 2002).

3. THE HARMONIZATION PROCESS

The deep-rooted differences in accounting regulations among European Union members were eliminated partially with the Fourth and Seventh Directives. Undoubtedly, the Directives seemed to improve comparability of financial statements in the European Union. On the other hand, the Directives were a result of a compromise which rested on allowing member states to maintain significant control over their accounting regulation. As a result, detailed provisions of national accounting regulation continued to be diverse. In Poland the accounting act was signed into law in 1994 and it already included some aspects of Fourth and Seventh Directives. Full compliance was achieved in the amendment of 2000.

In 1995 the European Union issued the *Communication* (1995) and stated that the Directives did not provide answers to all the problems facing preparers and users of financial statements, as well as accounting standard-setters. The *Communication* considered several proposals to solve that problem. Tightening cooperation with IASC (International Accounting Standards Committee) was thought to be the best solution. The decision to adopt International Accounting Standards (IAS) was confirmed in the *Financial Services Action Plan* (1999). It stated that the IAS were the best benchmark for financial reporting that might help to develop a common capital market in the EU. Meanwhile, several Member States, including Germany but not France or Poland, allowed listed companies to use IAS as a basis for their consolidated financial statements.

The final critical step in the harmonization process was the publication of EU Regulation No. 1606/2002, according to which consolidated financial statements of listed companies for the period beginning on or after 1 January 2005 had to be prepared on the basis of International Financial Reporting Standards endorsed by the European Commission. There is also an option in Regulation No. 1606/2002 for member states to allow other classes of companies to use the IFRS. In Poland this includes companies which: prepare to be listed on a regulated market in any country within the European Economic Area, or are part of a capital group, and the parent company reports on the basis of IFRS, or are a division of a foreign company that reports on the basis of IFRS. When Poland joined the European Union in 2005, all the *acquis communautaire* had already been incorporated into the national law. Although accounting practice is still heavily influenced by the requirements of tax law and a macro-uniform model is preferred for small and medium enterprises, the evolution of accounting law had prepared the ground for the adoption of the IFRS (Jaruga et al., 2007). At the same time commercial law and the securities laws were developed on the basis of the laws used in Germany.

4. EFFECTS OF IFRS IMPLEMENTATION. RESULTS FROM FORMER STUDIES

Some early research on the effects of mandatory IFRS implementation focused on the financial statements content (Ineum Consulting, 2008), changes in assets valuation (Cormier, Demaria, Lapointe-Antunes, & Teller, 2009; Jeanjean & Stolowy, 2008,) and financial ratios (Lantto & Sahlström, 2009), as in order to comprehensively research the effects of new accounting standards for capital market longer series of historical data were needed. The early research suggests that the introduction of the IFRS caused substantial changes in financial reporting so in consequence significant changes in relations between accounting information and market valuation might be expected.

Studies also that if a company decides to implement IFRS voluntarily, the effects will be different, because the company probably has economic incentives to do so, e.g. lower cost of capital. Voluntary implementation of IFRS may be also a sign of higher investor orientation and a better working corporate governance system in company. Further, research provides evidence that earnings management magnitude is on average higher in countries using the continental model of financial reporting with low investor protection rights, compared to countries using the Anglo-Saxon financial reporting model with high investor protection rights (Hung, 2000; Leuz, Nanda, & Wysocki, 2003). Van Tendeloo and Vanstraelen (2005) concluded that German companies following IAS and those applying German accounting regulations do not show significant differences in earnings management. By contrast, Bartov, Goldberg and Kim (2005) found that earnings relevance in companies that apply IAS was higher than in companies following German accounting regulations.

There is a growing number of studies examining if the target of improved usefulness of financial statements was attained due to implementation of IFRS. Most of them find a positive impact of IFRS mandatory implementation on the usefulness/quality of financial information disclosed by companies. Barth, Landsman & Lang (2008) find that use of IAS/IFRS by companies from 21 countries show positive impact on accounting information quality. They compared companies applying IFRS with their counterparts using non-U.S. domestic standards. They measured the quality of accounting information using the following proxies: less earnings management, more timely loss recognitions and more value relevance accounting amounts. These features are also characteristics of high earnings quality. The proxies for accounting information quality used by Barth, Landsman & Lang (2008) were the following: variance of the change in net income, the ratio of the variances of the change in net income to the variances of the change in cash flows, the correlation between accruals and cash flows, and the frequency of small positive income. They considered earnings that reflect losses on a more timely basis as being of higher quality.

There also exists a strain of research on value relevance changes of accounting information after IFRS implementation. Research based on the biggest European countries sample conducted by Macías & Muiño (2011) provided mixed results on value relevance of accounting data after implementation of IFRS. In some countries increase of correlation between model valuation and market valuation was observed, while in some countries the opposite effect was noted. The results could have been affected by changes of economic cycle. Other research indicated nonlinearity of the changes (Clarkson, Hanna, Richardson, & Thompson, 2011). Positive results were observed in the research focused on the elements that were changed to the biggest extent after implementation of IFRS: goodwill presentation, intangibles embracing R&D expenses and fixed assets (property, plant and equipment) valuation in fair value revaluation model (Aharony, Barniv, & Falk, 2010). It appeared that in countries where similar valuation methods were similar to IFRS, even before its mandatory implementation, these elements were more relevant for shares valuation. On the contrary, in countries where other valuation methods were used, their significance grew after IFRS implementation.

Research on Polish market reaction on the changes of accounting standards showed lack of significant changes in the association between returns and earnings after IFRS adoption

(Klimczak, 2011). The study was based on the abnormal returns model, which showed a high degree of fit both before and after IFRS adoption. The companies that implemented IFRS were valued higher before the mandatory IFRS adoption, however the effect vanished later. The results indicate that the effects of IFRS adoption are determined by firm-specific factors, rather than shared in the whole population. This is in line with arguments raised by Ch. Leuz, who states that institutional differences are more far reaching than financial reporting, therefore it should not be expected that changes in accounting standards will lead to by themselves actual changes of companies preparing financial statements (Leuz, 2010).

There is a growing number of studies examining the impact of mandatory and voluntary IFRS implementation around the world. Based on the sample of 353 French companies Zéghal et al. (2011) found that mandatory adoption of IAS/IFRS is associated with a reduction in the earnings management level. This research ends with the conclusion that implementation of IAS/IFRS by French companies reduces the use of discretionary accruals and therefore increases earnings quality. Yip and Young (2012) results suggest that mandatory IFRS adoption improves cross-country information comparability by making similar things look more alike without making different things look less different. They are also in line with Horton, Serafeim and Serafeim (2013) conclusions that after the mandatory IFRS implementation, forecast accuracy and other measures of the quality of the information environment improved significantly. They also found that the effect was more evident for mandatory adopters.

There are also few studies on the effects of mandatory IFRS implementation in new EU-members, including Poland. Some light on this topic is shed by the studies of Jaruga et al. (2007). The Jaruga et al. (2007) study showed that mandatory IFRS implementation caused in some cases enormous changes of earnings. According to Jaruga et al. (2007) differences in earnings prior and after IFRS implementation appeared mainly due to the application of regulations of IFRS 3, the de-recognition of intangible assets, and the decrease of accounting income as result of recognition of expenses relating to share-based payments or lower revenues due to long deferred payments.

Dobija & Klimczak (2010) carried out a study of the effects of the evolution of accounting regulation in Poland between the years 1997 and 2008. Their results show that a high degree of value relevance was achieved early, although after mandatory IFRS implementation Polish companies were valued higher, relative to their accounting performance, then before. Other research showed also that the above mentioned relation depends on ownership structure of the companies, and better valuation model had higher fir for companies that had big shareholders not connected with company board as well with big shares packages owned by company board members (KorczaK & Korczak, 2009).

Michalak, Waniak-Michalak and Czajor's (2012) study looked at the impact of the mandatory implementation of IFRS on earnings quality of companies listed on the Warsaw Stock Exchange in years 1999–2010. They use earnings persistence and accruals magnitude as the proxies of earnings quality and examine companies that prepare consolidated financial statements both before and after mandatory IFRS adoption. They document a weak positive influence of mandatory IFRS implementation on earnings quality.

5. HYPOTHESIS AND METHODOLOGY

On the basis of the literature review we can expect that the harmonization of financial reporting through the mandatory implementation of the IFRS leads to a reduction of the cross-country differences between the information content of financial statements. Furthermore, economic integration of Poland with the European Union leads to a convergence of prices, including stock values. Therefore, we begin with the null hypothesis, which we then attempt to reject:

H0: There are no significant differences in the parameters of accounting-based valuation models between comparable companies listed in Poland, Germany and France in the period after mandatory IFRS implantation

Since the goal of this study is to determine if significant differences in valuation model coefficients exist between Polish companies and companies listed in Germany and France, we design the study to minimize the probability of type II error. First of all, we use a sample matching algorithm to select samples of German and French companies which would be comparable in terms of size and sector with the Polish companies studied here. Thus, we control for structural differences between the three countries, which could cause valuation coefficients to diverge. Secondly, we estimate three alternative models: the levels model of Ohlson (1995), the scaled form of the Ohlson model (MTBV model) and the returns model (Easton and Harris 1991). This allows us to reduce the probability of errors resulting from model misspecification. Each model was expanded by adding interactions of the main accounting variable – residual income (RI), residual return on equity (RROE), and net income scaled by market value (SX) – with dummy variables representing the country of listing. The three models are as follows:

Levels Model:

$$MV_{it} = u_i + \beta_{10}BV_{it} + \beta_{11}RI_{it} + \beta_{12}DEU_i * RI_{it} + \beta_{13}FR_i * RI_{it} + Controls_{it} * RI_{it} + Controls_{it} + \varepsilon_{1it}$$

MTBV Model:

$$MTBV_{it} = u_i + \beta_{21}RROE_{it} + \beta_{22}DEU_i * RROE_{it} + \beta_{23}FR_i * RROE_{it} + Controls_{it} * RROE_{it} + Controls_{it} + \varepsilon_{2it}$$

Returns Model:

$$R_{it} = u_i + \beta_{31}SX_{it} + \beta_{32}DEU_i * SX_{it} + \beta_{33}FR_i * SX_{it} + \beta_{34}SDX_{it} + Controls_{it} * SX_{it} + Controls_{it} + \varepsilon_{3it}$$

where MV_{it} stands for market value of equity, BV_{it} stands for book value of equity, RI_{it} stands for residual income, $MTBV_{it}$ stands for the market-to-book-value ratio, $RROE_{it}$ stands for residual return on equity equal to ROE_{it} minus cost of equity capital, RI_{it} stands for total shareholder return over the fiscal year, SX_{it} stands for net income scaled by beginning of period market value, SDX_{it} stands for the first difference in net income scaled by beginning of period market value, DEU_i and FR_i are dummy variables denoting observations for companies listed in Germany and France respectively, u_i stands for the firm-specific intercept. Note that there is no dummy variable for companies listed in Poland, because the Polish sample is treated as the base.

The financial statements and market valuation data were collected from the Infinancials database. Market value is measured at the end of the reporting year in line with arguments presented by Szafranski and Klimczak (2013). Book value and net income data (Infinancials fields 4041 and 3045) and other financial statement data are standardised as provided by Worldvest Base Inc., which increases the comparability of financial statement information. Residual income and residual return on equity is calculated using a flat cost of equity capital rate at 8%.

We begin sample selection by limiting the time span to the years 2005-2011, that is after the mandatory adoption of IFRS by stock-listed companies. However, IFRS adoption is required only of companies preparing consolidated statements, so we limit the sample to such companies. Further, we remove companies with market capitalization lower than €40 million as of 2011, because data for such companies is sparse in the database. We also remove companies belonging to sectors SIC 6 (finance, insurance and real estate) and SIC 9 (public administration). This sample selection procedure yielded 169 companies listed at the Warsaw Stock Exchange. However, we needed to drop data for 17 companies, for which the sample matching algorithm was unable to find comparable companies in the other two countries, and a further 12 companies for which data availability was insufficient, which resulted in 139 Polish companies being included in the final sample.

The comparable samples of German and French companies were selected by applying the `psmatch2` algorithm (Leuven & Sianesi, 2012), which uses propensity score matching. The propensity scores were calculated on the basis of average market capitalization within each comparable group. The groups were formed by partitioning the sample according to the decile of average market capitalization and two-digit SIC sector codes. However, this approach allowed us to identify comparables for a third of the sample only, so we needed to broaden the search criteria. We present the results of sample matching in Table 1 according to the match level. If a comparable company was identified within the same decile/sector group, the match level was coded as 1. If a comparable was not found, the search was broadened by two deciles of average market capitalization and the results coded as level 2. Level 3 was assigned if a match was found after further broadening the search to the one-digit SIC code instead of two. Once a company was marked as a comparable it was removed from the pool.

Table 1. Number of companies matched per match level.

Match level	Germany	France
1 – the closest	51	59
2	26	49
3 – the farthest	69	49
Total	146	157

Table 2 presents descriptive statistics for each country sample, which makes the results of sample matching apparent. Comparable companies from the German market are of similar size as the Polish sample. The French sample contains a number of relatively large companies, but the difference is much smaller than before the application of sample matching. We carried out the Mann-Whitney test for the difference in the distribution of each variable between the samples both before and after matching. Results showed that the matching algorithm reduced the differences in market capitalization, book value and net income. Differences in the return on equity ratios, leverage and balance sheet composition persisted, which lead us to include these characteristics as control variables. Note that the statistics in Table 2 are presented in Euro for the readers' convenience, but estimations are performed on data in the national currency to avoid the effect of changes in exchange rate on the distribution of variables in the Polish sample. The bottom section of Table 2 contains the full set of variables used in the study, while the top sections contain only a selection of variables for each country sample.

The models include interactions with control variables which allow us to control for specific factors that affect valuation model coefficients. `SMALL` is a dummy variable assigned value 1 if a company falls in the two bottom deciles of market capitalization. `NEGEARN` is a dummy variable assigned value 1 if a company returned a loss in a given year. `ACCRUALS` is a measure of the intensity of accruals components in net income, calculated as the difference between net income and net cash flows from operations scaled by net income. Note that in the `MTBV` model the numerator is limited to net cash flows from operations because the inclusion of net income caused the `ACCRUALS` variable to be correlated with `RROE`. Two additional variables are included because their values vary significantly between country samples because of differences in company strategies. `GOOD` represents the proportion of intangible assets to total assets. `LEVERAGE` stands for the debt to equity ratio. The medians of the two variables are lower by more than a half in the Polish sample as compared to the German and French samples.

Correlation tables for the three models (Table 3) show that the `MTBV` model is characterised by the lowest correlation between independent variables. Significant correlation is found only between residual return on equity and two of the interactions. In the levels model the correlation between the two main variables, book value and residual income, is caused by the absence of a deflator. On the other hand, in the returns model it is the deflator that causes correlation to appear, because the variance of market values is high enough to shadow the variance in the scaled variable.

Table 2. Descriptive statistics in ['000 EUR]

	Mean	SD	N	Min	p25	p50	p75	Max
Companies listed at the Warsaw Stock Exchange								
MV	471 142	1 268 881	754	5 453	35 600	99 925	313 969	10 948 603
S	612 908	1 979 074	754	12 278	67 825	145 088	392 086	25 965 598
MTBV	1.87	1.70	754	0.29	0.81	1.30	2.22	8.36
RROE	0.05	0.20	754	-0.72	-0.04	0.03	0.13	0.71
R	0.17	0.78	668	-0.76	-0.37	-0.01	0.46	2.46
Matched sample of comparable companies listed at Deutsche Boerse (DEU)								
MV	420 206	1 229 011	877	5 453	37 400	96 426	288 019	15 480 000
S	621 521	1 858 858	877	12 278	79 785	178 303	402 766	23 282 236
MTBV	1.83	1.48	877	0.29	0.92	1.39	2.32	8.36
RROE	0.01	0.23	877	-0.72	-0.06	0.02	0.11	0.71
R	0.13	0.56	848	-0.76	-0.23	0.05	0.37	2.46
Matched sample of comparable companies listed at Euronext Paris (FR)								
MV	836 440	3 431 104	975	5 453	43 529	110 682	324 390	29 173 138
S	1 213 280	4 501 098	975	12 278	82 354	177 287	499 619	36 351 000
MTBV	1.87	1.50	975	0.29	0.87	1.43	2.39	8.36
RROE	0.03	0.19	975	-0.72	-0.04	0.03	0.12	0.71
R	0.09	0.53	937	-0.76	-0.25	0.04	0.33	2.46
Full sample								
MV	590 672	2 326 274	2 606	5 453	39 828	104 263	312 598	29 173 138
BV	322 537	1 071 929	2 606	517	33 240	71 527	183 260	13 712 000
RI	11 269	89 517	2 606	-344 134	-2 949	1 391	7 728	875 600
S	840 428	3 154 737	2 606	12 278	77 252	166 385	436 939	36 351 000
TA	955 923	3 964 282	2 606	11 415	74 000	167 007	476 848	47 931 000
MTBV	1.86	1.55	2606	0.29	0.87	1.38	2.31	8.36
RROE	0.03	0.21	2606	-0.72	-0.05	0.03	0.12	0.71
R	0.13	0.62	2453	-0.76	-0.28	0.04	0.36	2.46
SX	0.05	0.15	2454	-0.62	0.02	0.06	0.10	0.44
SDX	0.03	0.19	2454	-0.46	-0.02	0.01	0.05	0.94
LEVERAGE	0.40	0.60	2606	0	0.03	0.18	0.49	3.33
GOOD	0.13	0.15	2606	0	0.02	0.08	0.21	0.57
ACCRUALS	-0.10	0.27	2477	-1.27	-0.18	-0.06	0.03	0.61

Variable names: MV is the market value of equity, BV is the book value of equity, RI is residual income, S is revenue from sales, TA is total assets, MTBV is the market-to-book-value ratio, RROE is the residual return on equity ratio, R is the total shareholder return over the fiscal year, SX is net income scaled by beginning of period market value of equity, SDX is the first difference in net income scaled by beginning of period market value of equity, LEVERAGE is the debt-to-equity ratio, GOOD is the proportion of intangible assets to total assets, ACCRUALS is the difference between net income and cash flow from operating activities scaled by net income.

Table 3. Correlation Matrix

Levels model						
	BV	RI	SMALL*	NEGEARN*	ACCRUALS*	
BV	1					
RI	0.4898	1				
SMALL*RI	0.0175	0.0563	1			
NEGEARN*RI	-0.0919	0.2688	0.1592	1		
ACCRUALS*RI	-0.0523	-0.0842	-0.1877	-0.4851	1	
MTBV model						
	RROE	SMALL*	NEGEARN*	ACCRUALS*	GOOD	LEVERAGE
RROE	1					
SMALL*RROE	0.5357	1				
NEGEARN*RROE	0.7316	0.5267	1			
ACCRUALS*RROE	0.0141	0.0272	0.1008	1		
GOOD	-0.0706	0.001	-0.0176	-0.0062	1	
LEVERAGE	-0.1364	-0.0727	-0.1591	-0.0122	0.0524	1
Returns model						
	SX	SDX	SMALL*	NEGEARN*	ACCRUALS*	
SX	1					
SDX	0.4424	1				
SMALL*SX	0.6284	0.2622	1			
NEGEARN*SX	0.8467	0.2533	0.5728	1		
ACCRUALS*SX	-0.6164	-0.1456	-0.3977	-0.7905	1	

6. RESULTS

The three models offer satisfactory levels of explanatory power. Estimation results (Table 4) show that the MTBV and the returns model performs better than the levels model in terms of the fraction of the cross-sectional variance which is captured by the model as opposed to the firm-specific intercept. In terms of time variance, the levels model shows a slightly higher R^2 than the returns model, while in the MTBV model the R^2 is lower by nearly a half.

The base valuation coefficient at the main income variable (*RI*, *RROE* or *SX*) varies between 3.2 and 4.2. This represents the value for the base sample, that is Polish companies. The valuation coefficient for the German sample is significantly lower in the MTBV model (by 1.6) and in the returns model (by 0.9). In the levels model the country-specific coefficient is insignificant although the value is similar. There is no evidence of the coefficient being different in the case of comparable French companies. Even though the value of the coefficient is large in the levels model, the standard error is large enough to render the coefficient insignificant.

The valuation coefficient is also affected by control variables, although results vary by the model. Small companies are valued lower relatively to other companies in the case of the levels and MTBV models, but not the returns model. Instances of negative earnings cause a significant decrease in the valuation coefficient in the MTBV and returns models. In fact, the coefficient is large enough to completely offset the base valuation coefficient. Accruals intensity has a significant negative impact on the valuation coefficient in the levels and returns model. An increase of one standard deviation causes the valuation coefficient to fall by 1.2 in the levels model and 0.4 in the returns model.

Table 4. Estimation results

	Levels model	MTBV model	Returns model
Dependent variable	MV	MTBV	R
BV	0.2973 (1.72)		
RI	3.1829 *** (3.54)		
RROE		3.4618 *** (6.10)	
SX			4.2247 *** (9.83)
SDX			0.4262 ** (2.81)
Interactions of country effects with the main performance variable			
DEU*	-0.9534 (-0.78)	-1.5773 ** (-2.77)	-0.8861 * (-2.09)
FR*	5.9046 (1.54)	-0.2353 (-0.41)	-0.7607 (-1.75)
Interactions of control variables with the main performance variable			
SMALL*	-3.8764 * (-2.35)	-1.3337 ** (-2.73)	0.1524 (0.57)
NEGEARN*	-2.6067 (-1.31)	-3.5623 *** (-5.96)	-5.9612 *** (-13.86)
ACCRUALS*	-4.328 * (-1.98)	-0.4402 (-1.70)	-1.4105 *** (-3.70)
Control variables			
NEGEARN	63 857 (1.11)	-0.5294 *** (-4.34)	-0.0588 (-1.03)
GOOD		-3.1616 *** (-4.06)	
LEVERAGE		0.3736 ** (2.98)	
R ²	0.3081	0.1791	0.2565
N	2470	2470	2299
Firms	442	442	412
Corr(u,Y)	0.7957	-0.1961	-0.2857
Rho	0.8994	0.5818	0.1731

Note: Table reports results of fixed effects panel estimation with robust standard errors. Intercepts are omitted. Interactions with the main accounting income variable (RI, RROE or SX) are denoted with an asterisk. The R² stands for within-R², Corr(u,Y) stands for correlation of firm-specific intercept with the dependent variable, Rho stands for the fraction of unexplained variance due to the firm-specific intercept. Significance levels: * p<0.05, ** p<0.01, *** p<0.001.

7. DISCUSSION AND CONCLUSIONS

The results indicate that the differences in valuation coefficients between comparable samples of Polish, German and French companies are smaller than one could expect when comparing a transition economy with two well-developed European economies. We can reject the null hypothesis of no difference in valuation coefficients only when comparing Polish and German companies, whereas we find no significant differences between Polish and French companies. Moreover, German companies are valued lower relative to their performance than the Polish ones. If we were to interpret this result as an indication of accounting quality, we could argue that the quality of Polish companies' accounting information is higher than in the comparable sample of German companies. Such a judgment would be premature however.

The difference in valuation coefficients between comparable samples of Polish and German companies can be attributed to a number of factors and need not be associated with financial reporting practice. First of all, Polish companies are characterised by high historical sales growth rates, hence current performance can be perceived by market participants as a signal of significant future growth in earnings. If the expectations of future growth are indeed higher for Polish companies than for their German counterparts, valuation coefficients would also be higher. Secondly, Poland is still classified as an emerging market, which affects the investment strategies of institutional investors. Market multiples used to be higher than in developed markets before the crisis, then fell rapidly in 2008 and have continued to match the developed markets since then. Perhaps surprisingly, the reduction of market multiples was welcomed by some domestic market participants who viewed it as evidence of the maturity of the Polish market. Finally, Polish companies are on average much smaller than German or French companies, but their information environment may be strong because local companies attract attention of domestic investors and the media, their relatively small size notwithstanding. The information environment of comparable companies from the other two markets may be weaker, because they are overshadowed by large companies.

In conclusion, our study shows that after IFRS adoption companies from a transition economy of Poland are not valued lower, relative to their accounting performance than companies from developed countries. Even though Poland is classified as an emerging country, the valuation coefficients are higher than for German companies and not different from valuation coefficients for French companies matched by size and sector. The results suggest that the mandatory adoption of the IFRS, coupled with other institutional changes and a maturing capital market, lead to a convergence of valuation model parameters. It may be also a proof that the European Union's goal to improve the usefulness of financial statements was at least partially attained.

The limitations of our study are associated with the use of matched sample study design, which precludes the generalization of our findings to the broader population of stock-listed companies. Thus, we cannot draw inferences as to the comparability of accounting information of Polish companies which were too small to be included in our sample. Neither can we generalize the findings to German or French companies other than those included in the matched samples. It is important to note, however, that the use of matched samples is a key method of assuring the internal validity of our findings.

Further studies may benefit from using the methodological approach adopted in our study which makes comparisons between emerging and developed countries meaningful by controlling for structural differences in company samples. We show that companies from an emerging country exhibit similar patterns of valuation as do similar companies from developed markets, hence future international comparative research could focus on comparable sections of markets, rather than study entire populations of companies covered in commercial databases. The methods of sample matching can be improved by using a larger number of characteristics, in particular the inclusion of more economic factors. Another challenge is to control time-varying economic factors which would hamper studies of the changes in valuation model coefficients between different periods, such as before and after the mandatory adoption of the IFRS.

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CORRUPTION, UNETHICAL BEHAVIOR AND CORPORATE CULTURE

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Abstract: *While the research of Dan Ariely et al. suggests that culture in general plays a minor role in supporting unethical or illegal behavior, it proves on the other hand that there is a contagion effect in groups. Today the discussion about the behavior especially in the banking sector seems to prove the fact, that unethical behavior needs to be embedded in the corporate culture. An action model of corruption developed based on a study by Tanja Radl in the German University of Bayreuth also emphasizes the importance of corporate culture as enabler of unethical behavior. Dan Ariely also suggests that the few "big" cases of fraud cause in the long run lesser damage than the millions of "little" day-to-day cases.*

I suggest that national culture also plays an important role. Based on what we might call a "national archetype" a certain behavior is acceptable in a society or not. Germany is in that matter in many ways still divided and therefore a good example to study a very different philosophical background and its effects on how to do business. To change this behavior it will be important to

- 1. Develop very clear and concise guidelines for corporate governance on EU level.*
- 2. Encourage businesses of all sizes to develop a corporate culture which awards ethical behavior and punishes violations of the corporate code of conduct.*
- 3. Establish political control systems to enable a fair competition in the marketplace especially in the financial service industry.*

Keywords: *Corporate Culture, Corruption, Unethical Behavior*

BROKEN MODELS, BROKEN DREAMS

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Abstract: *The presenter worked for nine years at the largest sovereign wealth fund in the world, and regularly met with fund managers and financial analysts who seldom used the models and analytical tools which were the standard fare of courses and training sessions offered by universities and other institutions. The question arises as to why there is such a divergence. The recent credit crisis, which sent shock waves through the financial system has perhaps sounded an alarm bell to the analyst community, and should be used to re-visit some of the materials being taught and models being used to determine their efficiency. The limitations of models such as the Dividend Discount Model (DDM), and the Capital Asset Pricing Model (CAPM), which includes Beta (β), to predict outcomes has long been known in the investment community. Some studies, such as Fama and French (1992) have called some of these items into question, but the debate rages on. Meanwhile, what is an analyst to do when he must make an investment recommendation?*

Keywords: *Predictions, Dividend discount models, CAPM, beta, credit crisis*

ACCOUNTING REGULATIONS AND THE WORLDWIDE GLOBALIZATION PROCESS: FROM ABSORPTION TO HARMONY IN AN EMERGING ECONOMY

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Abstract: *Research literature and developments in the international arena of accounting standard setting seem to be hanging on the existence and manifestation of a certain process of bringing national accounting systems to a common denominator. First debates in this area talked about international harmonization while nowadays we also refer to international convergence, endorsement and even condorsment. The process itself is an extremely complex one that requires the consideration of a series of determinant factors. Our paper focuses on a qualitative and quantitative analysis of the manner in which Romanian accounting regulations evolved, while also considering the IFRS/IAS developments. Performing such an analysis by covering three decades of accounting developments led us to considering another form of accounting harmonization that was not yet identified through prior accounting research literature. We argue for spontaneous harmonization also acting as a form of de jure harmonization and not only of de facto harmonization as documented by van der Tas (1988). The main objective of our study is to investigate the manner in which the adoption of the international set of accounting regulations takes place at the level of a national accounting system. More precisely, we consider the case of IFRS/IAS and Romanian accounting regulations. An interesting differentiation is found when analyzing the implications of ad litteram or non ad litteram adoption. In this regard we develop an Absorption Degree Index (AD Index) in order to quantify the comparability degree when considering an ad litteram approach, and a Harmonization Degree Index (HD Index) considering a non ad litteram approach. We found the Romanian environment to be offering an interesting setting when debating the underpinnings of the harmonization process, as well as when testing the new approaches which we are proposing. The obtained results document both the manifestation of spontaneous harmonization in the area of formal harmonization and significant differences between the comparability degree of two sets of accounting regulations quantified through the two approaches being discussed. Considering the existence of spontaneous harmonization in the area of de jure harmonization and the ad litteram and non ad litteram approaches to quantifying the comparability of accounting regulations offer useful insights for standard setters, especially in the context of the worldwide globalization process nowadays already being put to the test.*

Keywords: *Absorption Degree, Harmonization Degree, Spontaneous de jure harmonization, Comparability, Romania*

ACCOUNTING IN THE MUNICIPAL NON-PROFIT ORGANIZATIONS

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Abstract: *This article concentrates on the classification and the assessment of accounting system in municipal non-profit organizations in the Czech Republic. The municipal non-profit sector is a special industry with many specifics. For that reason, accounting systems in municipal non-profit organizations calls for very special accounting approaches, methods and accounting software. Besides theoretical principals of accounting systems in municipal non-profit organizations is this article supplemented by case study by Prague Botanic Garden in the Czech Republic in the field of efficiency. In this study to lay some common ground there are firstly described principals of municipal sector in the Czech Republic followed with the accounting and funding system, and then it is applied economic analysis for measuring effectiveness of this organization. The presented case studies inform us about accounting systems in municipal organizations and present this as necessary to capture the complex indicators for municipal non-profit organizations in the Czech Republic.*

Keywords: *Accounting system, Municipality, Non-profit organization, Efficiency*

1. INTRODUCTION

Enterprise and business activities form the basis of current market economy of the Czech Republic. It is obvious that the concept of entrepreneurship is rightly associated with profitable entities, since the aim and motive of business is profit. At the same time this fact is related to detecting the economic reality of business entities with a legislative setting of accounting systems and their legal implementation. However, non-profit organizations also build their organization on economic fundamentals, and therefore depiction of the economic reality of these non-profit entities is entirely a matter of principle throughout the economy. But at the same time the philosophy of fulfilling the social mission is determining in these entities, of course, by the implementation of market principles and the achievement of at least minimum profit as a condition of permanent existence of a non-profit organization.

The non-profit sector in the Czech Republic is a phenomenon that appears to be one of the largest in the counties of Central Europe. In terms of the structure of financing sources, the non-profit sector ranks among the countries with a dominant role of the proportion of funds coming from their own activities. This fact highlights the importance of entrepreneurship in non-profit organizations. However, current non-profit sector of the Czech Republic works in the economic and legislative environment that is characterized by specific features for the sector. These specifics along with the current legislation of non-profit organizations creates quite complicated and confusing environment for the implementation of business activities. Complexity, ambiguity and difficulty to meet all legal standards can become a demotivating factor in the decision process of non-profit organizations whether to initiate business activities or expand the scope of business. Despite these difficulties, it can be stated that the own resources gathered from the implementation of business activities mean financial support and ensure the future development of non-profit organizations.

The basic condition for successful business of non-profit organizations in the current market environment is the implementation of modern management principles (strategic management and marketing management), because without the knowledge and use of modern management

principles non-profit sector implementing business activities will not succeed in the hypercompetitive economic environment these days. Modern principles of management of business activities in the non-profit sector based on knowledge of marketing management and strategic management are effective and also bring their effects to the sector. Management business activities of the non-profit sector in the Czech Republic is a challenge for the future of non-profit organizations that aims to build a successful organization with a sufficient financial and intellectual base allowing a higher quality to accomplish its essential mission .

2. ECONOMIC AND LEGISLATIVE FRAMEWORK OF ACTIVITIES OF NONPROFIT SECTOR OF THE CZECH REPUBLIC

At the beginning of the consideration of business activities in the non-profit sector it is necessary to define the nature and role of this phenomenon. The non-profit sector can be viewed from the economic and sociological standpoints. Economic view states that the non-profit sector along with the profitable sector is the part of the national economy and as such it is further divided into public and private subsectors and a household sector. Another view is closer to the social science, since it looks at the non-profit sector as an element of society, or rather as an innermost expression of civil society as an entity that wants to participate actively in political power and public debate on key social issues.

The non-profit sector, the non-profit organizations are concepts which many people are a little worried about, because they have only an indicative idea of what they mean. No current legislation in the Czech Republic covers these terms. In general terms they are common, because they include a number of organizations in various fields. To some extent, the issue of non-profit organizations is dealt under the law on income tax. The non-profit organization is an organization that was not founded or established for the purpose of business, but it is an organization in whose activities either the state and society, or a certain group of people are interested. It is founded to pursue its activities in favour of those who had an interest in its establishment. A greater emphasis is put on the importance of the results of the main activities, although in the current market economy financial background and incomes of the non-profit organization become essential for the functioning of the organization. Non-profit organizations are therefore legal persons having their founder, they are founded according to various laws and they subject to registration in areas designated to them by the laws under which they are established Non-profit organizations are as well allowed to implement business activities, which are subjected to generally applicable legislative directives, but also those laid down by their founder.

3. ACCOUNTING SYSTEMS IN ORGANIZATIONS

Accounting is methodically integrated system of information on the activities of the entity in the financial statements.¹ Accounting has faithfully and honestly reflect economic (material and financial) situation of an entity. Accounting and processing are governed by generally accepted principles which are set out in the Accounting Act and the Czech accounting standards. The obligation to keep records required by law No. 563/91 Coll., On books.

The main task of accounting is serving as a monetary truthful information from which we get the true picture:

- the property situation in the organization (a specific type of property, its valuation and wear),
- the sources on which the assets were acquired (the amount of equity and liabilities and their detailed structure),

¹ KOVANICOVÁ, D., KOVANIC, P. (1996): Treasures hidden in the accounts. Part I – How to understand financial statements. Praha: Polygon, 1, Prague, pg. 40–52.

- the financial situation of the company (profit, loss, solvency).

Accounting in itself is not the goal and end preparation of the financial statements, the diagnosis itself does not determine the state of the company, used to transmit the information to enable users to make appropriate decisions. For accounting treatment must be followed by an analysis of its results. The actual aggregate output accounts still do not provide a complete picture of the economic and financial situation of the company, its strengths and weaknesses, risks, trends and total quality management. Information about the financial situation they are presented to users in the form of financial statements.

With the information necessary for financial analysis is designed primarily financial accounting, which leads to the audited and published accounting (financial) statements that should provide a "true and fair view of the accounts and the financial situation of the unit" (see Accounting Act No. 563/1991 Sb., as amended). Incorrect assessment of the financial trustworthiness are caused misleading, although the audited financial statements. Financial scandals of major U.S. corporations (Enron, WorldCom, Tyco) were important lesson and created the need for stricter legislation on corporate governance (corporate governance) in the U.S.²

Model accounting in the Czech Republic and abroad

The globalization of the economy is accounting harmonization aimed at removing differences between the various types of regulation. For the financial accounting, the harmonization takes place in individual countries, which is implemented unification of accounting, the external regulation and international accounting standards, the so-called self-regulation. Unification of Accounting (so-called external regulation) is a management accounting by the State or its chambers. Self-regulation is management accounting as a single entity that is governed by the applicable accounting standards of the country, which for us are the Czech accounting standards. Harmonization within the European Community constitutes a single business environment, including accounting, taxation and legal standards for capital company.³

Tools harmonization of the accounting system are the directives of the European Union and the International Accounting Standards and International Financial Reporting Standards (IAS / IFRS). Then put in a global scale we are talking about the global concept of U.S. GAAP, where there is a mutual cooperation IAS / IFRS and U.S. GAAP, and because of the globalization of capital markets.

Czech accounting

The legal basis is given by the Czech Accounting Act No. 563/1991 Coll., Accounting, connected sets of implementing regulations for different types of entities. Accounting law is common to all types of entities, individual specifics are then taken into account in the implementing regulations and Czech accounting standards that provide specificity in defining the content of some items in the balance sheet, profit and loss, supplements and chart of accounts. Accounting Act allows to keep accounts in full and simplified format.

European Union Directive

European Union Directive can be defined as binding rules for all Member States of the European Union, which requires their incorporation into accounting systems. By agreeing to the Member States shall become binding standards and have a fixed term implementation. In the field of accounting were processed as follows:

- EU Fourth Directive, which harmonizes the financial statements, including general rules for the preparation of financial statements,

² DAMODARAN, A. (2000): *The Dark Side of Valuation*, available online at <http://pages.stern.nyu.edu/~adamodar/pdfiles/papers/HighGrow.pdf>

³ Novotný, P. (2007): *Principles of Accounting*. Prague, VŠEM, 1, pg. 140.

- Seven EU directive, which concerns the financial statements and Volkswagen Group holding group,
- EU Eighth Directive, which concerns the audit of financial statements.

International Accounting Standards

IAS / IFRS are best practices that allow for individual problem areas more acceptable solutions. It can be used as national requirements or as a benchmark for countries developing their own requirements. Each country has its own internal regulations to which they should be implemented or accounting standards may be accepted as binding law. Among the problem areas addressed by IFRS / IAS can sort - Presentation of Financial Statements, by, inventories, cash flow statement, accounting policies, changes in accounting estimates and errors, events after the balance sheet date, construction contracts, income tax, land, buildings and equipment leasing, revenue effects of changes in foreign currency exchange rates, borrowing costs, earnings per share, impairment of assets, provisions, contingent liabilities and contingent assets, intangible assets.

US GAAP

U.S. GAAP generally accepted accounting principles or accounting principles of accounting, which are a set of rules, conventions and procedures that are necessary for accounting practice at the time. It is here applied the common law in their work. They are not binding regulations formulated and are not dictated by any particular accounting procedures.

4. INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS (IPSAS)

4.1 Survey of IPSAS

A lot of information you can get in manual „Survey of International Public Sector Accounting Standards“. It is based on English original of manual „IPSAS Summary“ published by Holland office of company Deloitte (www.iasplus.com). This book consists of description of basic differences between standard IPSAS and present Czech legacy in the field of accounting reporting in public sector, that means units as regional autonomy whole, contributed organizations, state funds and organizational parts of state.⁴

The whole world, especially the Europe Union, unambiguous is directed at the system giving more relevant and reliable information for management accounting units and mutually increased transparency and quality accounting and finance reports and public sector informations for external users. International public sector accounting standards are based on International financial reporting standards that are concerned on commercial

Survey of IPSAS consists of the Code of ethics for Auditors and Professional Accountant is based on Principal Changes of Substance from the 2007 Handbook.

⁴ Deloitte (2013): available online at http://www.deloitte.com/view/cs_CZ/cz/services/audit/98ae16ac9be75210VgnVCM100000ba42f00aRCRD.htm

File	File Description
IPSAS 1	Presentation of Financial Statement
IPSAS 2	Cash Flow Statement
IPSAS 3	Accounting Policies, Changes in Accounting Estimates and Errors
IPSAS 4	The Effects of Changes in Foreign Exchange Rates
IPSAS 5	Borrowing Costs
IPSAS 6	Consolidated and Separate Financial Statement .
IPSAS 7	Investments in Associates
IPSAS 8	Interests in Joint Ventures
IPSAS 9	Revenue from Exchange Transactions
IPSAS 10	Financial Reporting in Hyperinflationary Economies
IPSAS 11	Construction Contracts
IPSAS 12	Inventories
IPSAS 13	Leases
IPSAS 14	Events after the Reporting Date
IPSAS 15	Financial Instruments: Disclosure and Presentation
IPSAS 16	Investment in Property
IPSAS 17	Property, Plants and Equipment
IPSAS 18	Segment Reporting
IPSAS 19	Provisions, Contingent Liabilities and Contingent Assets
IPSAS 20	Related Party Disclosures .
IPSAS 21	Impairment of NonCashGenerating Assets ..
IPSAS 22	Disclosure of Financial Information about the General
IPSAS 23	Revenue from NonExchange Transactions
IPSAS 24	Presentation of Budget Information in Financial Statements
IPSAS 25	Employee Benefits
IPSAS 26	Impairment of CashGenerating Assets

Fig. 1. IPSAS_survey of IPSAS

Cash Basis IPSAS, that means also Financial Reporting Under the Cash⁵, editorial Board's Notes of the Translation and review of other documents.

5. CLASSIFICATION OF ACCOUNTING SYSTEM IN NON-PROFIT ORGANIZATIONS IN THE CZECH REPUBLIC

Software Gordic for public sector

Typical representative of software products for state administration is Gordic intended especially for state administration and self-government. It is determined for treatment of economical and administrative agent including keeping registers. For software is typical high variability, low demands for technical equipment, flexibility and speed that react to changes in legacy, methodology, technological trends and users demands. To cover needs and demands of all users help a big frequency agents and three lines of products that safe work to users from individuals up to big institutions as ministries.

⁵ Cash Basis IPSAS, International Federation of Accountants (2013): Available on-line at <http://www.ifac.org/public-sector/projects/cash-basis-ipsas-disclosure-recipients-external-assistance>

For big institutions is recommended the information system GINIS working in multilayer architecture www terminal – client – server. This system is typical with monitoring of each document from entrance to exit to the system included also to the treatment with any agent and its connection to accounting operations in first documents (contracts, invoices, statements of accounts and regulations). It is higher quality attitude to problems of agents in organization – every record in database is based on strictly registered and approval document. It is suitable for efficient institution management in the recording and identification of all operations carried out by individual employees, which contributes to the fulfillment of their personal responsibilities. GINIS ® system is characterized by high security class C2.

Another line of products are applications in architecture client- file server, the brand name of this product line is GORDIC ® G0. These are applications designed for small and medium-sized organizations.

The third product line is called GORDIC ® G3. These are applications in architecture client- file server are they are also designed for small and medium-sized organizations.

The Resolution No 1027 of 10.10.2001 issued by the Government of the Czech Republic tasked to unify the environment in the area of personnel information systems in administrative offices. The aim is not only to improve the flow of information in the field of personnel work, but also raise the quality and efficiency of work in personnel departments of administrative offices. The company GORDIC Ltd presented solutions PERGAM and PERGAM-SEC, which won in a public tender launched by ÚVIS. This solution is technically identical with the information system GINIS ®, i.e. it works in a multilayer architecture www-terminal client-server and it is characterized by high class security, including meeting the conditions of the Act 148/1998 in Collection of Laws on the Protection of Classified Information.

Software Vema for state and private organizations

Vema is the business information system that offers complete solution in the field of information systems for management of human resources, economics and logistics in state organizations and also in private organizations in Czech Republic. The product is offered by VEMA joint-stock company with the seat in Brno and branch offices in Prague, Olomouc, Ceske bud2jovice and Plzen. Vema is divided to three divisions:

- division ***Product*** that cares for application of development and production of information system,
- division ***Services*** insure complete service connected with implementation and application using by the costumers,
- division ***Business-Operation*** engages in economic, business and administrative agenda and marketing.

The company Vema has on the Czech market an exclusive position. This company with revenues more than 100 mil. Kč belongs to the leading Czech producer of the firm information system. It develops and ensure Best-of-Breed ERP solution specialized to the field of economy, logistics with wide spectrum of organizations as from the number of employees as from area. You can also to rent VEMA software through internet that is very demanded. Nowadays about 250 companies use ERP system by means of ASP model and that ranks company VEMA among first place in this category in the Czech market.⁶

Small excursion to history is also very interesting. The company VEMA was set up with the program computers and programming limited liability company in 1990. Then follows first distribution of application for wage processing PAM Vema. In 1991 was established first economic informational system EKOS Vema. Two years later was introduced application Attendance. In 1995 the products offer was extended with net application and new products Personal management and Education. In 1998 was first installed electronic attendance system. In

⁶ Vema: Specialist in human resource management, economics and logistics, (2013) <http://www.cvis.cz/hlavni.php?stranka=novinky/clanek.php&id=991> dne 21.9.2013

2000 was established joint-stock company VEMA and three years later was used portal application using. In 2005 was firstly used providing application with service ASP. In 2008 VEMA offered the outsourcing in wage processing.

Vema gained a lot of certificates, for example ČSN EN ISO 9001:2009, ČSN ISO 10006:2004⁷, TOP 100 ICT companies⁸, Brno TOP 100⁹, WEB TOP 100¹⁰

6. CASE STUDY – BOTANICAL GARDEN OF THE CITY OF PRAGUE

Application performance management contributory organization Botanical Garden of the City of Prague

This chapter is practically focused on the issue of the performance of organizations using the financial indicators. In terms of financial indicators specifically focuses on the role of different performance areas where using the tools of financial analysis, indicators of profitability, liquidity, activity or complex using the Altman Z-score or index IN05 assess the financial situation contributory organizations of the City Botanic Gardens. Prague. As a suitable representative of the municipal non-profit company. What explanatory power have reporting financial accounting, which is being conducted using software Gordic and more or less conducive to EU standards, just outlines the following text.

The major characteristics of the financial health of the organization is surely return (from lat. Return on Italian or rent) or return as the ability to generate profit from investments. This indicator is one of the main criteria of business. In the financial analysis, it is one of the elementary concepts and indicators of financial health. The most frequently used indicators belong return on assets ROA (Return on Assets), which informs us about the effectiveness of the management organization with assets. Furthermore, the return on equity ROE (Return on Equity), which informs us of the return on equity and, ultimately, return on sales ROS (Return on Sales) as the company's ability to transform inventory into cash. The device monitoring devices, these indicators move as follows:

Return (%)	2012
ROA	0,05
ROE	0,05
ROS	0,3

Fig. 2. Return Botanical Garden of the city Prague¹¹

Because the return on assets (over 7% of the recommended value) and return on sales (over 8%) is in the low ranges, it means that the device does not use its assets optimally and fails to transform inventory into cash. Return on equity could be higher, which is a task for the management of the organization.

In addition to profitability is also very often assesses liquidity organization, which is an indicator of solvency of the company. Liquidity ratios derived solvency of the firm as the ratio between short-term current assets (redeemable for cash) and short-term liabilities (debts payable in the near future, usually within 1 year). In addition to the evaluation of liquidity can certainly add an indicator of net working capital, also called operating or performing capital. It is calculated as the difference between current assets (excluding long-term debt) and current liabilities,

⁷ VEMA Company (2013): Certificates of Vema, Available at vema.cz/default.aspx?categoryID=Vema_web1.1182&var&language=cs

⁸ Top 100 ICT firms (2013): Available on-line at <http://www.czechtop100.cz/>

⁹ Top 100 (2013): Available on-line at <http://www.ibrno.cz/hlavni-strana-anketa-brno-top-100>

¹⁰ Information about WebTop100 (2013): Available on-line at <http://archiv.webtop100.cz/soutez/vysledky>

¹¹ Prague Botanical Garden (2012): own processing Botanical Garden of the city Prague Annual Report 2012, Available at http://www.botanicka.cz/buxus/docs/pdf/vyrocn_zprava_2012.pdf

respectively debt because the value of short-term liabilities must also assign conventional loans with banks and short-term financial assistance. Specifically, the situation is reflected in the following table.

Liquidity	2012
Current liquidity	2,51
Quick liquidity	2,18
Instant liquidity	1,68
Net working capital	17 615 123

Fig. 3. Liquidity Botanical Garden of the city Prague¹²

In evaluating liquidity ratios can be said that the organization has adequate solvency. According to figures working capital and also has sufficient reserves to cover operating assets.

Another important area that are interested in any organization is its activity. Management of assets in contributory organization explicitly part of the tasks of corporate governance as a problem in terms of sales, default on receivables may have an adverse impact on its ability to meet its obligations, then it is more debt, which complicates the process of conversion of capital in the company, binds more capital and reduces its ability to generate sales and profits. The indicators are then inventory turnover, i.e. how long it takes for a turnover of monetary forms over productive resources back into monetary form (e.g. 30 days indicates a very favorable development) or the turnover of receivables or recovery time and turnover time of payment as payment duration relief organizations. Also noteworthy is the indicator of turnover cycle of money, which can be recommended oscillate around 0 or the negative value that informs us that the collection takes place at shorter intervals than our payment obligations.

Activity /Days/	2012
Inventory turnover	14
Turnaround claims	22
Turnaround liabilities	44
Turning cycle of money	-8

Fig. 4. Activity Botanical Garden of the city Prague¹³

In conclusion, application of methods of financial analysis funded organization were used aggregate indicators of financial health ratings, and an indicator of bankruptcy, Altman Z-score model. Summary evaluation is shown in Table 5, where the indicator shows the value of very good financial health. It appears, therefore, that the applicability of the principles of financial indicators for this organization is satisfactory.

Model	2012
Z- skóre	26,90

Fig. 5. Z-score Botanical Garden of the city Prague¹⁴

The benefits of working for theory and practice, in particular finds (e):

- mapping issues related to accounting systems in budgetary organizations with applications in assessing the performance of these organizations in the Czech Republic,

¹² Source: own processing Botanical Garden of the city Prague Annual Report 2012.

¹³ Source: own processing Botanical Garden of the city Prague Annual Report 2012.

¹⁴ Source: own processing Botanical Garden of the city Prague Annual Report 2012.

- verify the applicability of the principles of performance management to charitable organizations,
- definition of knowledge about the relationship of performance management and accounting systems,
- create a material that further development may be published as a monograph in performance management contributory organization.

7. CONCLUSION

The post on the topic classification of accounting systems in municipal non-profit organizations deals with the connection of two closely related spheres - economic and financial, in the sphere of municipal non-profit organizations. It mentions the main methods of accounting systems in NGOs Czech Republic, performance management and provides practical examples. In this "two-dimension" it is necessary to remember that every step will be the contribution made organizations, will have a direct impact on all of us.

The reform of economic systems is absolutely necessary step, but each expert confirms that it is not always understood by the general public. There is therefore no doubt that the economic sphere associated with carrying containers, but each step is necessary to bear in mind that affects every citizen who requires economic-financial service care. Only those who are able to offer attractive services to ensure economic results. Even the non-profit sector and market mechanisms adopted almost in its entirety, including the principles of performance management. Prospects that open municipal non-profit companies based on market economy principles, guarantees safety, quality, and last but not least, the high values of indicators.

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RE-THINKING THE CONCEPTS OF GOODWILL AND INTANGIBLE ASSETS

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Abstract: *This paper discusses one of the most controversial aspects related to the theory and practice of International Accounting: the difference between Goodwill and Intangible Assets. The issue needs proper theoretical discussion, as it is important to offer a clear definition of both concepts, Intangible Assets and Goodwill. Unfortunately the distinction is not always clear to both academics as well as practitioners. This may be because, in the course of time, various elements previously encompassed under the definition of Goodwill are nowadays classified as Intangible Assets (i.e. trademark). Whereas others (i.e. motivation of the workforce, list of clients) are classified either ways in the literature.*

This paper intends to discuss the evolution of both concepts, critically examine the state of the art of the literature and formulate recommendations.

Keywords: *Goodwill, Intangible Assets, Control*

INTRODUCTION

This paper studies one of the most important and controversial aspects characterizing contemporary Accounting theories and practices: the difference between Intangible Assets and Goodwill. Assets and Goodwill represent two different concepts and, from a theoretical point of view, Goodwill is something else than (Intangible) Assets are (Johnson and Patrone, 1998; Carrara et.al., 2005; Nobes and Parker, 2010; Alfredson et.al., 2009). However, the distinction is not always necessarily clear if we look at the conceptual definitions and at practical items which need to be classified under either of these categories. The issue is of importance for accountants, because Goodwill and Intangible Assets concur to the determination of the value of a company in a different way. Moreover, as for the preparation of financial statements, the treatment of the two categories is different, for example internally generated Goodwill cannot be inserted in the Balance Sheet (whereas, on the contrary, internally generated Intangible assets can be inserted in the Balance Sheet). In addition, the distinction is relevant also to tax-payers, as the tax regime of various countries treats Intangible Assets and Goodwill differently. Identifying a clear conceptual distinction between these two voices of the Balance Sheet, and consequently and unambiguously classifying items under these categories, represent an important task for accountants and a challenge for theoreticians and practitioners.

In reality, the distinction between Intangible Assets and Goodwill is still representing an open issue, despite a certain amount of attention already put by scholars (Jenkins and Upton, 2001; Nobes and Parker, 2010). The aim of this paper is to contribute to the process of solving one of the most controversial aspects of contemporary accounting. This paper will refer to the definitions and examples provided in the International Financial Reporting Standards (IFRS). The paper will refer to those definitions of concepts valid at the 1st January 2013.

This paper will be organized in the following way. Section 1 will discuss the concept of Goodwill and its practical applications, section 2 will introduce the concept of Intangible Assets. Conclusions and References will follow.

Section 1. Goodwill

IFRS 3 indicates that (<http://eifrs.ifrs.org/eifrs/bnstandards/en/2013/ifrs3.pdf>):

The acquirer shall recognise goodwill as of the acquisition date measured as the excess of (a) over (b) below:

(a) the aggregate of:

(i) the consideration transferred measured in accordance with this IFRS, which generally requires acquisition-date fair value (see paragraph 37);

(ii) the amount of any non-Controlling interest in the acquiree measured in accordance with this IFRS; and

(iii) in a business combination achieved in stages (see paragraphs 41 and 42), the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree.

(b) the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed measured in accordance with this IFRS.

33 In a business combination in which the acquirer and the acquiree (or its former owners) exchange only equity interests, the acquisition-date fair value of the acquiree's equity interests may be more reliably measurable than the acquisition-date fair value of the acquirer's equity interests. If so, the acquirer shall determine the amount of goodwill by using the acquisition-date fair value of the acquiree's equity interests instead of the acquisition-date fair value of the equity interests transferred. To determine the amount of goodwill in a business combination in which no consideration is transferred, the acquirer shall use the acquisition-date fair value of the acquirer's interest in the acquiree in place of the acquisition-date fair value of the consideration transferred (paragraph 32(a)(i)). Paragraphs B46–B49 provide related application guidance.

IFRS 3 considers Goodwill to be a residual, namely the value of the company which exceeds the combined value of the Assets. Hence, a company is considered to embed an additional value not caught by the combination of the value of the single Assets (Thurm, 2012). This additional value would represent something that cannot be re-conducted under the definition of Assets. Otherwise, logically, it should be classified as an Asset itself (even if some authors still insist in considering Goodwill as an Intangible Asset, see Jerman and Manzin, 2008). Therefore, a specific element or item contributing to the creation of value of a company is classifiable in the Balance Sheet either as an Asset or as (part of) Goodwill (Alfredson et al., 2009). Finally, this means that classifying Goodwill as an Asset, as it is sometimes done (Jerman and Manzin, 2008), represents a mistake as, following the definition of IFRS, Goodwill is something else than an Asset.

According to the definitions and logic introduced above, those elements representing Goodwill are still capable of contributing to the formation of value of a given company, however they do not respect those characteristics that would allow their classification as Assets. Goodwill would appear as something hidden and not directly visible (Murdoch, 2009) At this stage, it appears of help to specify what an Asset is. For this purpose, we refer to the Framework of IFRS. Assets are defined as: *An asset is a resource Controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity (IFRS Framework, 4.4.a).* It is therefore logical to deduct that those elements classifiable as Goodwill do not match these characteristics. A detailed discussion follows below.

It is clear that Goodwill represents a resource. A resource, is "The total means available to a company for increasing production or profit" (<http://www.thefreedictionary.com/resource>). It is clear that Goodwill is perceived by acquirers as a mean useful to increase profits or production, otherwise it would make little sense that sometimes acquirers pay a sum higher than the combined value of the Assets. Goodwill is considered as a mean or an item useful to contribute to the achievement of the aims of the company, which can be the maximisation of profits, of wealth of shareholders or of market shares (see Dunning and Lundan, 2008). It appears also quite logical that an acquirer expects an economic benefit to accrue from it. There is still a further element that

must be considered in order to better appreciate the difference existing between Goodwill and (Intangible) Assets: an entity (company) must have the capacity to Control the Asset. This latter element, namely Control, is understood as the capacity of a company to use a specific resource or dispose of it (Alfredson, 2009). A company has Control on a resource if the use of the resource depends on the will of the Company and not on favourable circumstances or on the will of other parties. This element seems of utmost importance in our discussion as, as we will discuss, it is exactly the lack of effective Control that allow accountants to classify certain items as Goodwill rather than as Intangible Assets.

Originally, before the very concept of Intangible Assets started to emerge and gain importance, a number of intangible elements were classified as Goodwill, as a certain tradition tended to restrict the classification of Assets to Tangible ones. Tangible Assets were/are considered to be easier to measure and their existence is beyond doubt (Nobes and Parker, 2010). Those invisible elements still concurring to the determination of the market value of a company were normally classified as Goodwill. This originally included items like the Brand value, the list of customers, the reputation of the company in the market, the capacity of the workforce to cooperate effectively and efficiently. In the course of time, a number of these items has been re-classified under the category of Intangible Assets. This because these very items were respecting the definition of Assets : they were a resource from which an economic benefit was expected, capable of being measured in terms of money value and under the Control of the company.

It is our idea that the requisite of Control is the discriminant factor that allows to have an idea regarding the real nature of various items. It appears nowadays clear that a company has the capacity to Control its own Brand. This because the use of a Brand is disciplined by law and normally any entity has the right to decide regarding the use of its own Brand. A similar logic underpins the classification of Softwares, which are intangible items sold in the market and whose legal use from a Third Party depends on a contract signed by the entity having the right to decide regarding the use of the softwares.

Other elements which still contribute to the formation of the value of a given company are of a different nature. For example, the good reputation of a company is certainly an element from which an economic benefit can be logically expected, as consumers are likely to prefer to purchase goods and services from a company with a good market reputation. It would eventually be possible to devise a method suitable to give a monetary value to the reputation of a company in the market. One may argue that such methods would probably lack in objectivity and reliability. However, this represents a common problem also for the determination of the value of financial instruments not listed in any market and for which there is not an objective market price or for the determination of the value of a Brand. It is reasonable to infer that, in view of the fact that accountants have devised methods for the determination of the value of unlisted financial instruments and Brands, then they would likely devise also a method suitable to evaluate items like reputation or list of clients. One may be critical of the possibility to measure objectively such items, but then we would need to rediscuss also the objectivity of the measuring methods of the value of assets like Brands or unlisted derivatives.

Nonetheless, there is a fundamental problem related to the incapacity from the side of the reporting entity to Control certain elements. The lack of effective of Control can justify a different accounting treatment. While a company can clearly dispose of its trademark, eventually forbidding the use from a Third Party, according to existing laws, an existing customer, not bound by any contractual obligation, may by its own will decide to conclude the cooperation. On the same token, the company does not have Control on other elements like for example Reputation. It is therefore not possible to classify these items as Assets. Still, these specific elements concur to the determination of the value of a given company, as an eventual purchaser would reasonably accept that the consideration includes also the value of these very elements not classifiable as Assets. It appears then useful to continue using the category Goodwill to account for them. Goodwill, then, would preserve its residual character, already recognised in IFRS, and represent the value of items

which, still concurring to the determination of the market value of a company, are not classifiable as Assets

INTANGIBLE ASSETS

Originally and for a long time, classical Accountants hesitated before accepting the very idea that Assets could also be Intangible. The very nature of Assets was supposed to lead to objective verification of their existence and a reliable determination of their value. These characteristics were considered to be more consonant with the nature of Tangible Assets. Tangible Assets are directly visible, their acquisition cost is determinable so that there is an objective basis useful to determine their value. Moreover, the market for Tangible Assets was more developed than that one for intangible assets. For a certain time, intangible items still able to carry a value, were subsumed under the classical Goodwill and not classified as Assets.

In the course of time, it became evident that specific intangible items were themselves representing a significant share in the determination of the value of a company (Lev, 2001; Nobes and Dumay, 2013) especially with the growth of high-tech companies. Moreover, their use was subject to the Control of the entity and an active market for Intangible Assets like Copyrights, Trademark was developing. Hence, certain intangible Assets, besides becoming more and more relevant to the determination of a company market value, were also respecting characteristics that allowed a separate classification from the bulk of Goodwill. This evidence reinforced the idea that also Intangible Items could be classified as Assets. There is a trend which indicates that the size of Goodwill is narrowing down, as more and more items have been included under the category of Intangible Assets.

IAS 38 indicates that items are classifiable as Intangible Assets when, among other already discussed conditions, they are separable. Hence, it could seem that the criterion for distinguishing Assets from Goodwill is that of separability. However, an Asset is classifiable as separable when it can be „i.e..... sold, transferred, licensed, rented or exchanged, either individually or together with a related contract.....“. We understand that the terms above, taken together, represent the capacity of the company to Control a specific item. Which, as discussed in the previous section, is a fundamental characteristic of Assets. Hence, a reading of IAS 28 confirms that the discriminant element allowing to distinguish Goodwill from Intangible Assets is the capacity of the entity to Control a specific item.

CONCLUSION

It appears that distinguishing Intangible Assets and Goodwill is possible. The determinant factor should be the possibility to Control a resource, which is a fundamental characteristic of Assets. This means that items like for example Reputation and List of Customers cannot be put under the Control of a company and therefore cannot be classified as Assets. Indeed, this appears to us as the real factor which allows to separate Goodwill from Intangible Assets.

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Useful websites

<http://www.thefreedictionary.com/resource>)

www.iasb.org

www.iasplus.com

THE IMPLEMENTATION OF IFRS BY LISTED COMPANIES IN ROMANIA – PAST, PRESENT AND FUTURE

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Abstract: *In Romania, starting with the fiscal year 2012, companies whose securities are admitted to trading on a regulated market are required to apply IFRS in preparing individual annual financial statements, in accordance with the Order of the Minister of Public Finance no. 1286/2012 regarding the approval of the Accounting Regulations in accordance with the International Financial Reporting Standards applicable to companies whose securities are admitted to trading on a regulated market. This research aims to present the status quo of the financial reporting under IFRS as at December 2012, as follows: companies covered by this regulation are identified; these companies are then analyzed by several criteria; the transparency of financial reporting is postulated, and this hypothesis is tested by identifying the IFRS financial statements as at 31 December 2012 that were made public by the companies in the sample; authors hypothesize the difficulty to restate the financial statements in accordance with the Romanian regulations, hypothesis tested by identifying where IFRS reports were published with delay. The results are interpreted in relation to the previous authors' research on the ability of IFRS implementation in Romania, carried out at another key moment – the issuance of the Order of the Minister of Public Finance 1121/2006 on the application of International Financial Reporting Standards which established mandatory application of IFRS for companies whose securities at the balance sheet date are admitted to trading on a regulated market and which prepare consolidated financial statements. Finally, based on the experiences of the past and on the current status quo, authors state future directions in terms of the capacity to implement IFRS in Romania.*

Keywords: *IFRS, listed companies, Romania, implementation capacity*

1. INTRODUCTION

Transparency on the capital market is currently a topical issue both nationally and internationally. On this background, the IFRS implementation is considered by regulatory bodies an instrument to increase transparency for current and future investors. Following this international trend, the Romanian legislation recently changed by expanding the IFRS implementation scope to individual financial statements issued by companies with securities accepted for trade on a regulated market. Starting with the fiscal year 2012, companies whose securities are admitted to trading on a regulated market are required to apply IFRS in preparing individual annual financial statements, in accordance with the Order of the Minister of Public Finance no. 1286/2012 regarding the approval of the Accounting Regulations in accordance with the International Financial Reporting Standards applicable to companies whose securities are admitted to trading on a regulated market. This research aims to present the status quo of the financial reporting under IFRS as at December 2012 in Romania, namely to identify the companies falling under the scope of this regulation are identified; to analyze this population by several criteria; to test the transparency of financial reporting identifying whether the IFRS financial statements as at 31 December 2012 were made public by the companies in the sample in time and what kind of audit opinion did they receive. The paper is structured as follows: first, the research design is briefly presented; then the relevant regulatory framework is described; the

fourth section details the results of the data analysis, while the final paragraphs include the comments and conclusions of the researchers.

2. RESEARCH DESIGN

The research methods used are empirical. Companies which fall within the scope of the new regulations were identified based on the data from the National Commission of Securities. A total of 67 was found, out of which two were eliminated from the analysis (one had the financial year end the 30th of September and one did not have financial information from the individual financial statements available). For each of the companies in the population, the following general and financial data was hand-collected from the website of the Bucharest Stock Exchange: listing tier, district, the corresponding code within the National Classification of Economic Activities, equity in 2012 and 2011, net turnover in 2011 and 2012, average number of employees in 2012 and 2011. All data collected are public. The primary data was grouped by tier, geographical area, activity, type of company (small, medium, large), equity, and net turnover. For a sample of 14 companies, the audit reports have been downloaded from the official websites of the entities. The audit report date was used as proxy for the date when financial statements were published. Moreover, the type of audit opinion issued was analyzed. The sample was chosen so that it includes at least one company from each category, depending on each of the criteria mentioned above.

3. REGULATORY FRAMEWORK

Recently, in June 2012, the Romanian Minister of Public Finance issued the Order 881/2012, which stipulates that starting with the financial year 2012, the companies the securities of which are accepted to be traded on a regulated market shall apply the International Financial Reporting Standards (IFRS) when preparing individual annual financial statements.

Additionally, in October 2012, the Minister of Public Finance also published the Order 1286/2012 for the approval of the accounting regulations in compliance with IFRS applicable to these trade companies.

According to Order 881/2012, IFRS represent the standards adopted according to the procedure stipulated in article 6, paragraph (2) of the EC Regulation no. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards. Consequently, the IFRS issued by IASB are to be applied as far as they had been adopted within the European Union, by regulations.

Companies affected by Order 881/2012 must ensure the continuity of their IFRS application even in case their securities at balance sheet date are not accepted to be traded on a regulated market anymore.

Trade companies falling within the scope of Order 881/2012 should restate, in compliance with IFRS, the data and information contained in the trial balance prepared for the year ended 31 December 2012 on the basis of the accounting regulations approved under Order 3055/2009 of the Minister of Public Finance. The resulting IFRS statements must be prepared in the national language (Romanian) and expressed in the national currency (RON).

4. COMPANIES FALLING WITHIN THE SCOPE OF THE NEW REGULATIONS

One of the objectives of the present paper is to identify the companies which fall within the scope of the new regulations. For this purpose, the first step was to thoroughly analyze the relevant legislation.

It was found that the legislation clearly states that the provisions of the Order 1286/2012 for the approval of the accounting regulations in compliance with IFRS do not apply to the following entities:

- credit institutions;
- non-banking financial institutions registered in the General Register and payment institutions and institutions that issue electronic money, as defined by law, which grant credit related to payment services and whose activity is limited to the provision of payment services, respectively issuance of electronic money and payment;
- Bank Deposit Guarantee Fund;
- entities that are authorized, regulated and overseen by The Insurance Supervisory Commission (*Comisia de Supraveghere a Asigurarilor – CSA*);
- entities that are authorized, regulated and overseen by the Supervisory Commission for the Private Pension System (*Comisia de Supraveghere a Sistemului de Pensii Private – CSSPP*);
- entities that are authorized, regulated and overseen by the National Commission of Securities (*Comisia Națională a Valorilor Mobiliare – CNVM*);

Order 881/2012 stipulates that companies' securities must be accepted to be traded on a regulated market. This regulated market is defined by Law no. 297/2004 regarding the capital market, with the subsequent amendments. Following the analysis of this law, authors concluded that the Bucharest Stock Exchange is the only Romanian capital market that fulfils the requirements of Order 881/2012.

5. DATA ANALYSIS

Companies falling within the scope of Order 881/2012 are **67 (sixty-seven)**. They form the total statistical population of the present research. Collecting financial data for each of these companies as at 31 December 2012 resulted into the fact that one company reports as at 30th of September. In case of another company, the financial statements disclosed on the website of the Bucharest Stock Exchange are the consolidated financial statements for the year end December 2012. These are not relevant for the present research, which focuses on **individual** financial statements prepared **as at 31.12.2012**. Therefore, these two companies have been eliminated from the population. For all other **65 (sixty-five)** companies, financial information as at 31 December 2012 in the same format has been disclosed.

In order to obtain a general view on these companies, the primary data has been systematized. The data volume has been compressed by means of statistical grouping. Following this grouping, the companies within the population have been separated into homogenous groups, depending on the variation of one characteristic or of several characteristics. From the perspective of the number of characteristics chosen, the researchers performed both a **simple** and a **combined** grouping. From the perspective of the content of the characteristics, the grouping was also performed depending on a **territorial characteristic**, on different **attributive characteristics** and on different **numerical characteristics**. The detailed results of the grouping are described in the following paragraphs.

First of all, according to the statistical organization of the Romanian territory, there are eight (8) development regions with an average population of 2.8 million people and 42 districts. The regions and the corresponding districts are:

- Region „I North-East” : districts Bacău, Botoșani, Iași, Neamț, Suceava, Vaslui;
- Region „II South-East”: districts Brăila, Buzău, Constanța, Galați, Vrancea, Tulcea;
- Region „III South”: Argeș, Călărași, Dâmbovița, Giurgiu, Ialomița, Prahova, Teleorman;
- Region „IV South West”: districts Dolj, Gorj, Mehedinți, Olt, Vâlcea;

- Region „V West”: districts Arad, Caraș-Severin, Hunedoara și Timiș;
- Region „VI North-West”: Bihor, Bistrița-Năsăud, Cluj, Maramureș, Satu-Mare și Sălaj;
- Region „VII Center”: districts Alba, Brașov, Covasna, Harghita, Mureș, Sibiu;
- Region „VIII Bucharest-Ilfov”: districts Bucharest and Ilfov.

The structure of the analyzed companies according to these regions is displayed in Table 1.

Table 1. Population's structure depending on the territorial characteristic

Region	Number	Percentage
I North-East	7	11%
II South-East	9	14%
III South	8	12%
IV South West	7	11%
V West	2	3%
VI North-West	10	15%
VII Center	8	12%
VIII Bucharest-Ilfov	14	22%
Total	65	100%

Source: own design

The General Requirements for the listing at the Bucharest Stock Exchange for all types of financial instruments are as follows: firstly, the instruments must be registered with the National Securities Commission (CNVM); secondly, they need to be transferable, dematerialized and fully paid.

In case of shares issued by domestic entities, the following requirements must be met, depending on the tier, as presented in Table 2.

Table 2. Requirements for the listing of domestic shares in the Bucharest Stock Exchange

	Tier I	Tier II	Tier III
free float	> 25%	> 25%	> 25%
free float held by at least	2000 owners	-	-
shareholders equity for the last financial year or anticipated capitalization	> 30 mil EUR	> 2 mil EUR	> 1 mil EUR
net profit	for the last 2 years	-	-
a bussiness plan	at least for the next 3 years	-	-
an executive summary to the admission prospectus	Yes	-	-

Source: <http://www.bvb.ro/Companies/Listing.aspx?t=2&m=bse>

The structure of the analyzed companies according to these three tiers is displayed in Table 3.

Table 3. Population's structure depending on the attributive characteristic “listing tier at the Bucharest Stock Exchange”

Tier	Number	Percentage
I	15	23%
II	49	75%
III	1	2%
Total	65	100%

Source: own design

Another grouping criteria for the analyzed companies was their type of activity. For this purpose, authors collected for each of the companies the corresponding code within the National Classification of Economic Activities (CAEN – *Clasificarea activităților din economia națională*). The CAEN code has four figures, whereas based on the first figure, authors identified the so-called **section** within the Classification and based on the first two figures, authors identified the so-called **division**. Generally, the sections are the following:

- Section A: Agriculture, Forestry and Fishing
- Section B: Mining and Quarrying
- Section C: Manufacturing
- Section D: Production and Supply of Electricity and Heat, Gas, Hot Water and Air conditioning
- Section E: Water Supply, Sewerage, Waste Management And Remediation Activities
- Section F: Construction
- Section G: Wholesale and Retail Trade; Repair Of Motor Vehicles And Motorcycles
- Section H: Transportation And Storage
- Section I: Accommodation And Food Service Activities
- Section J: Information And Communication
- Section K: Financial And Insurance Activities
- Section L: Real Estate Transactions
- Section M: Professional, Scientific And Technical Activities
- Section N: Administrative And Support Service Activities
- Section O: Public Administration And Defence; Social Security in the Public System
- Section P: Education
- Section Q: Human Health And Social Work Activities
- Section R: Shows, Cultural Events and Entertainment
- Section S: Other Service Activities

The companies falling within the scope of the Order 881/2012 belong to the following sections, as presented in Table 4 below.

Table 4. Population's structure depending on the attributive characteristic “code within the National Classification of Economic Activities”

Section	Number	Percentage
B Mining and Quarrying	3	5%
C Manufacturing	44	68%
E Water Supply, Sewerage, Waste Management And Remediation Activities	2	3%
F Construction	5	8%
G Wholesale And Retail Trade; Repair Of Motor Vehicles And Motorcycles	4	6%
H Transportation And Storage	7	11%
Total	65	100%

Source: own design

In the European Union, companies are classified in the following four categories, depending on their number of employees: micro enterprises, small scale enterprises, medium enterprises and large enterprises. Micro enterprises are those that employ up to 9 people. Small enterprises employ between 10 and 49 people. Medium enterprises have between 50 and 249 people. Large enterprises are thus defined as having 250 or more employees.

According to this classification, the companies in foreground of the present research focuses are to be grouped as shown in Table 5.

Table 5. Population's structure depending on the attributive characteristic “enterprise type”

Type	Number	Percentage
micro-enterprise	0	0%
small enterprise	5	8%
medium enterprise	19	29%
large enterprise	41	63%
Total	65	100%

Source: own design

Besides the average number of employees based on which the above grouping was performed, financial data was also collected from the website of the Bucharest Stock Exchange, namely: shareholders equity for the financial years 2011 and 2012, as well as net turnover for the same two periods. However, these figures correspond to the financial statements prepared not in accordance with IFRS, but in accordance with the Romanian Accounting Standards (Order of the Ministry of Public Finance 3055/2009).

For grouping purposes, only the figures for 2012 (as current year) were taken into account. The amounts were originally expressed in the national currency (RON) and were converted into EUR by using the exchange rate as at 31st of December 2012 (4.4287 RON/EUR). Prior to this grouping according to numerical characteristics, authors analyzed the population by computing different indicators, both for equity and for net turnover, namely: the maximum, the minimum, the standard deviation, the mean, the median etc.

Table 6. Population's structure depending on the **numerical** characteristic “equity”

Equity (in €)	Number	Percentage
1. under 0	7	11%
2. 0–15,000,000	22	34%
3. 15,000,000–30,000,000	17	26%
4. 30,000,000–45,000,000	3	5%
5. 45,000,000–60,000,000	5	8%
6. 60,000,000–100,000,000	6	9%
7. over 100,000,000	5	8%
Total	65	100%

Source: own design

Following this analysis, in order to avoid potential void intervals, the following ranges have been chosen based on the characteristics of the population: in case of **equity**: negative equity; positive equity, but less than 15,000,000 €; between 15,000,000 € and 30,000,000 €; between 30,000,000 € and 45,000,000 €; between 45,000,000 € – 60,000,000 €; between 60,000,000 € and 100,000,000 €; over 100,000,000; in case of **turnover**: under 10,000,000; between 10,000,000 € and 30,000,000 €; between 30,000,000 € and 50,000,000 €; between 50,000,000 € and 100,000,000 €; between 100,000,000 € and 250,000,000 €; between 250,000,000 € and 1,000,000,000 €; over 1,000,000,000 €. Tables 6 and 7 contain the stratification of the population according to this intervals.

Table 7. Population's structure depending on the **numerical** characteristic “net turnover”

Net turnover (in €)	Number	Percentage
1. under 10,000,000	25	38%
2. 10,000,000–30,000,000	15	23%
3. 30,000,000–50,000,000	9	14%
4. 50,000,000–100,000,000	6	9%
5. 100,000,000–250,000,000	5	8%
6. 250,000,000–1,000,000,000	3	5%
7. over 1,000,000,000	2	3%
Total	65	100%

Source: own design

The grouping presented so far may be referred to as **simple grouping**, which offers a concise and at the same time detailed view on the companies that must prepare individual financial statements in accordance with IFRS starting 2012. Additionally, researchers also performed a **combined** grouping, by combining the above mentioned characteristics.

By grouping the data first according to type of activity (section) and then by type of enterprise, the following results came up, as follows. Companies that activate in “B Mining and Quarrying” are solely large enterprises. All three types of enterprises (small, medium and large) are to be found in “C Manufacturing”, “F Construction” and “G Wholesale And Retail Trade; Repair Of Motor Vehicles And Motorcycles”. There are no small enterprises in “B Mining and Quarrying” and “H Transportation And Storage”. To section “E Water Supply, Sewerage, Waste Management And Remediation Activities” belong two extremes: one large company and one small one.

Similarly, the data was grouped first according to region and then by type of activity (section). This grouping revealed the following facts. The greatest variety of activities is to be found in the central region (all types of activity except for “E Water Supply, Sewerage, Waste Management And Remediation Activities”) and in the region Bucharest-Ilfov (activities from sections B, C, E, F, G, less “H Transportation And Storage”). The only region where there are solely companies from one area of activity is the South-Western region – with seven companies operating in the manufacturing industry.

Another combined grouping of the data was performed as follows: first depending on the type of enterprise (whereas the key characteristic was the number of employees) and then depending on the level of shareholders equity. This analysis revealed that five large companies, one medium enterprise and one small one have negative equity. The equity of most small companies is positive and less than 15.000.000 euro. 68% of the medium companies have an equity of less than 15.000.000 euro, while in case of 21% of such enterprises, the equity ranges from 15.000.000 to 30.000.000 euro. In case of large enterprises, the equity is differentiated, belonging to all seven intervals: 12% of the companies – under 0; between 0 and 15,000,000 € – 15%; between 15,000,000 € and 30,000,000 € – 32%; between 30,000,000 € and 45,000,000 € –

7%; between 45,000,000 € and 60,000,000 € – 10%; between 60,000,000 € and 100,000,000 € – 12%; over 100,000,000 € – 12%.

Likewise, companies were then grouped after two criteria: type and net turnover. Consequently, it was shown that the majority of small enterprises have a net turnover of less than 10,000,000 euro, as do medium enterprises have. In the case of large enterprises, turnover ranges from the smallest to the highest turnover in the population. Almost one third have a turnover between 10,000,000 and 30,000,000 euro, while a fifth report between 30,000,000 and 50,000,000 euro. Just two big companies reported a net turnover of more than 1,000,000,000 euro.

Following the above-described analysis, a sample of 14 companies was extracted, so that there is at least one company from each category: region, type, net turnover, equity, and section. In case of each company, the audit report on the individual financial statements prepared in accordance with IFRS has been downloaded from the official website of the company. Usually, the audit report was published in the section with information for investors, together with the IFRS individual financial statements. The date of the audit report was then collected, and the type of audit opinion issued was identified. Table 8 below presents this data:

Table 8: Audit report date and audit opinion for the sample

No.	Tier	Region	Type	Net turnover	Equity	Section	Audit report date	Opinion type
1	II	VII Centru	large	3. 30,000,000-50,000,000	3. 15,000,000-30,000,000	B	25.03.2013	qualified opinion; 10 issues presented as basis + 2 notes in a separate paragraph
2	I	VIII București-Ilfov	large	7. over 1,000,000,000	7. over 100,000,000	B	21.03.2013	unmodified opinion
3	II	I Nord-Est	medium	1. under 10,000,000	2. 0-15,000,000	C	22.03.2013	unmodified opinion
4	II	III Sud	large	5. 100,000,000–250,000,000	1. under 0	C	26.04.2013	adverse opinion; 3 issues presented as basis
5	I	IV Sud Vest	large	6. 250,000,000–1,000,000,000	7. over 100,000,000	C	26.03.2013	unmodified opinion
6	II	VI Nord-Vest	medium	1. under 10,000,000	2. 0–15,000,000	C	27.03.2013	unmodified opinion
7	II	VIII București-Ilfov	large	4. 50,000,000–100,000,000	5. 45,000,000–60,000,000	C	21.03.2013	unmodified opinion
8	I	VIII București-Ilfov	large	2. 10,000,000–30,000,000	4. 30,000,000–45,000,000	C	15.03.2013	unmodified opinion
9	II	III Sud	small	1. under 10,000,000	2. 0–15,000,000	E	no date available	unmodified opinion
10	I	VII Centru	large	1. under 10,000,000	1. under 0	F	25.03.2013	unmodified opinion
11	II	V Vest	large	4. 50,000,000–100,000,000	2. 0–15,000,000	G	19.03.2013	unmodified opinion
12	I	VII Centru	large	4. 50,000,000–100,000,000	3. 15,000,000–30,000,000	G	29.04.2013	unmodified opinion; emphasis paragraph
13	I	II Sud-Est	large	2. 10,000,000–30,000,000	6. 60,000,000–100,000,000	H	14.03.2013	unmodified opinion
14	III	VIII București-Ilfov	large	3. 30,000,000–50,000,000	1. under 0	C	25.04.2013	adverse opinion; 17 notes as basis for the opinion; one paragraph of emphasis

Source: own design

All companies in the sample provided to the public the individual financial statements prepared in accordance with IFRS. The deadline for submitting the IFRS financial reporting was the 30th of April 2013. The audit report date served as proxy for the date of the financial statements, which is not made available to the public. However, research found that all audit reports were issued within the legal timeframe for the submission of the audited individual statements. Therefore, it can be reasonably assumed that all IFRS financial statements were also submitted on time. Most of the audit opinions are unmodified. However, there are two adverse opinions, both for companies where the insolvency procedure was open. From the 14 companies analyzed, only one received a qualified opinion.

6. COMMENTS AND CONCLUSIONS

The IFRS implementation in Romania is a gradual process. 2006 the Ministry of Public Finance issued the Order 1121, which stipulates that companies with securities accepted for trading on a regulated market prepare consolidated financial statements in compliance with IFRS. Additionally, the National Bank of Romania issued an order in 2010, according to which banks will give up the local accounting standards and will make the transition to IFRS for the individual financial statements. 2012 the Order 881 was published, based on which the IFRS implementation is expanded to individual financial statements of companies listed on the Bucharest Stock Exchange. According to Order 1121/2006, companies could opt for IFRS, but starting with the financial year 2012, the application of IFRS becomes compulsory as requested by Order 881/2012. In the authors' opinion, the logical and natural evolution of the IFRS implementation in Romania, in case of public interest entities, is that in the following periods, the IFRS scope will be extended to individual financial statements of other public interest entities such as insurance companies, companies that activate in the private pension system, national companies and entities. Of course, the speed of this evolution depends on the implementation capacity of such entities and their availability to assume the costs related to the IFRS implementation.

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APPLICATION OF IFRS IN PRACTICE – ISSUES AND OBSERVATIONS

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Abstract: *In this presentation the author will discuss several issues and challenges, which the preparers in Central Europe face when applying the IFRS standards. The author discusses the needs of financial statement users and compares them to the requirements and complexity of selected IFRS standards. The author will present several examples of areas and issues with practical impact on the preparers, including the treatment of business combinations under common control, put options over minority interest and own equity instruments, fair value measurement of certain non-financial assets and impairment calculations. The author will conclude by a brief review of the future developments of IFRS standards and their practical impact on the companies applying them.*

Keywords: *Central Europe, IFRS, practical issues*

PERCEPTIONS OF CZECH PROFESSIONAL ACCOUNTANTS ON CURRENT TRENDS IN INTERNATIONAL AND CZECH ACCOUNTING

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Abstract: *Central and Eastern European (CEE) countries are generally considered as developed market economies with environment close or similar to Western Europe and are also worthy for investment opportunities and research conducting. Despite of these similarities, however, their accounting models may differ from those used in developed economies. This paper focuses on the Czech Republic as one of the representatives of CEE region. It is the country with traditional linkage of accounting system to tax system and application of prudence principle in accounting. That is why fair value it is not such widely applied like under IFRS practices. Main objective of this paper is to find out the perception of the professional accountants on current trends in international accounting and how it might influence local Czech accounting practices. For this reason there was employed a questionnaire survey as a research tool. Results show the positive attitude of Czech professional accountants towards current trends in international accounting.*

Keywords: *accounting harmonization, Czech accounting practices, IFRS, professional accountants' perceptions*

1. INTRODUCTION

The process of accounting convergence and the issues related to the implementation of IFRSs worldwide are topics of much interest recently for standard setters, researchers and practitioners. Previous studies on IFRSs application documented an increase in comparability, transparency and quality of financial reporting (Jermakowicz, 2004). Significant impact on the companies' reported equity, increasing volatility of results and a diminishing degree of conservativeness were reported (Jermakowicz, 2004; Jermakowicz & Gornik-Tomaszewski, 2006; Callao et al., 2007). Also, previous studies analyzed the obstacles and difficulties in the application of full IFRSs (Larson & Street, 2004; Jermakowicz & Gornik-Tomaszewski, 2006), and the manner in which these standards are applied in different countries (for example Delvaille et al., 2005).

The national characteristics, i.e. each country's accounting culture and traditions, have developed over (a long) time in close relationship with the political, social and economical environment of each of them, influencing the way in which IFRSs are applied. Factors such as the role of the State, the type of legal system in place, the preferred providers of finance, the relationship between accounting and taxation, the culture, or the role of the accounting profession significantly influence accounting practices (Alexander et al., 2006; Nobes & Parker, 2008). Also, previous research indicated that the lack of political will, rooted in local culture and a strong national outlook prevent a truly harmonized accounting framework (Callao et al., 2007), that a magnitude of differences exists between countries and high costs to eliminate them (Jermakowicz & Gornik-Tomaszewski, 2006); that local traditions exercise a strong influence on the implementation of new concepts, and that tax and legally-based orientation hinder the harmonization process (Larson & Street, 2004; Vellam, 2004).

Measurement in financial accounting is one of factors which determines the quality and reliability of presented information. Solution of measurement issues is one of the key problems analyzed within current basic research in financial theory. Applied principles of measurement and

their regulations are interdependently correlated with the informational needs of external users (especially investors) and internal users (managers). Owners of the company may behave as external users (e.g. minority shareholders) or as internal users. Requirements on content of accounting information given by the used accounting (and measurement) method are strongly connected not only with the group of users (internal versus external) but also with economic environment. Actual economic environment strongly affects the requirements for measurement requested from users.

Upon economic boom there can be seen higher optimism of investors which leads towards requirement of measurement of all accounting items at fair values, which mainly represent current market prices of assets (Bonaci et al., 2010). Using this concept means the turn from the prudence principle and conservative historical costs concept in financial accounting. Moreover fair value concept in financial accounting leads to higher tendency of revaluation assets or liabilities affecting profit or loss of the company.

Upon economic recession users reevaluate their views on accounting methods, especially the measurement bases. Economic recession evokes the renaissance of conservative approaches in measurement, especially the applicability of prudence principle. Confidence in financial market upon recession is thrilled; there can be seen strong price swings. Swings in market prices of financial instruments or breakdown of real estate market may also evoke valid doubts whether the fair value concept (and market price is the most reliable evidence) is really the most objective and most reliable approach suitable for wide spectrum of users of accounting information (Müllerová et al., 2011).

After the period of recession economy tends to break up strict conservative rules and principles because of the pressure of the investors' requirements; there can be seen divergence from the prudence principle towards measurement based on actual market prices (or so called fair values). This evolution was visibly seen during last decades, not only at international level (standards IFRS and US GAAP) but also at national level (requirement to measure certain assets at fair value given by Czech Accounting Act). As a good example shall be stated the essential material of IASB (International Accounting Standards Board) prepared by group of Canadian experts which dealt with the measurement of assets and liabilities upon initial recognition and declared the divergence from historical costs measurement towards fair value concept. Quite important was also the common discussion paper of IASB and FASB (Financial Accounting Standards Board) which dealt with unification of fair value concept in IFRS and US GAAP (Cairns, 2006).

We think that the tendency of fair value measurement results from the investors' pressure: the main objective for investors was capital spillover and maximization of short-term profit. It is impossible to ignore the fact that all these requirements were strongly connected with economic boom conditions.

Too "optimistic" approach applied upon economic boom is based on fair value approach (Strouhal et al., 2010). The high value of assets which is given by active market or it is based on the estimates in case that active market does not exist, leads towards rising equity as well as balance sheet sum and in case of revaluation through profit or loss also towards fictive profits which can be distributed to owners. It shall be also stated that the estimates of fair values for non-financial assets, but also for certain financial assets (e.g. shares) used to have low level of reliability because of subjective estimates of valuator or based on mathematical models which are connected with restrictive assumptions. On the other hand the approach based on accounting conservatism and prudence principle in recession periods may (jointly with inflation) lead towards erosion of company's substance and deepen and prolong the recession.

2. RESEARCH DESIGN

Czech Republic as a typical representative of emerging economy from CEE area with the traditional linkage of accounting system to tax system and application of prudence principle in accounting. That is why fair value it is not such widely applied like under IFRS practices.

Main objective of this paper is to find out the perception of the professional accountants on current trends in international accounting and how it might influence local Czech accounting practices. For this purpose there was prepared a questionnaire survey.

This survey was conducted among selected Czech companies in spring 2013. The research was targeted on companies with clear audit opinion and questionnaire was sent to 4,082 companies. The return rate was 9.1 % and we analysed 371 valid questionnaires.

The survey (conducted online via Google Forms) had two parts:

- identification part (legal form of company, region where company operates, major activity and furthermore the information related to finance and accounting),
- analytical part which could be divided onto two more parts: questions related to company's behaviour (3 questions), questions related to perceptions on selected accounting issues (7 questions).

Structure of respondents was as follows:

- legal form of business
 - 134 JSC, 232 Ltd, 5 other companies
- region
 - mainly Southern Moravia (85), Prague (83), Northern Moravia (52), Central Bohemia (41)
- major activity
 - 207 production companies, 72 trade companies, 92 service companies
- turnover
 - 152 companies with turnover lower than 250 mil. CZK; 70 companies with turnover higher than 1 bil. CZK
- total assets
 - 79 companies with total assets lower than 100 mil. CZK; 61 companies with total assets higher than 1 bil. CZK
- employees
 - 285 companies with less than 250 employees; 16 companies with more than 1,000 employees (one company with more than 25,000 employees)
- statutory auditor
 - 98 companies audited by "Big 4" group, 38 companies audited by global auditing firm, 235 audited by Czech auditing firm
- accounting framework
 - 249 companies applying Czech GAAP only, 28 companies applying IFRS only; 94 companies applying both rules (primarily Czech GAAP, for reporting to parent company IFRS)

3. RESULTS AS A BASIS FOR CONCLUSION

First set of questions was related to companies' real behaviour. We tried to analyse the areas of depreciation policies, impairment and provision issues and also the popular area of financial securities and derivatives.

1 – Applied methods for depreciation

accounting – linear	317	85.4%
accounting – DDB	8	2.2%
accounting – SYD	5	1.4%
accounting – by performance	18	4.9%
tax depreciation only	53	14.3%

Majority of companies, as expected, prefer linear accounting method. However, there shall be highlighted that almost 15 % of tested companies is computing tax depreciation only. This is a surprising finding as it cannot be expected that tax methods lead towards true and fair view despite all analysed companies have clear audit opinion.

2 – Impairment

yes, tax only (bad-debts)	67	18.1%
yes, bad-debts	294	79.2%
yes, inventories	196	52.8%
yes, non-current assets	89	24.0%
not applied	7	1.9%

As expected, the most popular title for impairment computation is the bad-debts provision, followed by impairment of inventories.

3 – Provisions

tax deductible	79	21.3%
yes, business risks	208	56.0%
yes, income tax	131	35.3%
not applied	87	23.4%

The most popular titles for provisions in Czech practice are business risks and income tax issues. Historical there was widely popular the provision on repair of tangible assets, which is still a tax deductible item (despite it is strictly prohibited by IFRS), however linkage of this provision to obligatory cash fund made it less and less popular in current practice.

Second part of this questionnaire survey dealt with the impact of current trends in international accounting and their possible spread to Czech accounting rules. Concretely there were discussed the issues of finance lease, fair value measurement, revenue recognition and also financial statements.

1 – Who Shall Report the Object of Finance Lease?

lessee	202	54.4%
lessor	169	45.6%

Under current Czech accounting legislature, it is a lessor who reports the object of finance lease within its financial statements. However, results show the willingness of companies to report this item rather under the IAS 17 treatment.

2 – Shall Be Investment Properties Measured at Fair Value under Czech Accounting Rules?

yes	284	76.6%
not	87	23.4%

Investment properties are not recognised as a specific category under Czech accounting legislature, and therefore shall be measured just at cost (like other non-current assets). From the results there is visible the willingness of the participants to apply fair value measurement for this category (like under IAS 40).

3 – Shall Be Long-Term Receivables and Long-Term Payables Measured at Amortised Costs under Czech Accounting Rules?

yes	244	65.8%
not	127	34.2%

Current accounting practices in the Czech Republic do not differ between long-term and short-term receivables or payables when discussing the issues of their measurement. All receivables and payables are simply measured at their nominal values. If comparing this treatment with IFRS, under IAS 39 (or IFRS 9 respectively) these items shall be measured at amortised costs. Based on the results, again shall be stated, that respondents prefer the IFRS treatment, i.e. 2/3 prefer to measure these items at amortised costs.

4 – Shall Be “Change in Inventories” Classified as Operating Revenue?

yes	175	47.2%
not (operating expense)	196	52.8%

Current Czech accounting legislature requires recognising “change in inventories” as internal revenues, however under IAS 18 this category does not fulfil the definition of revenues. Results do not show the significant trend in preferences, however, under in-depth analysis, smaller companies reporting under Czech accounting rules and having Czech auditor prefer the current treatment as operating revenues.

5 – Wider Spread of Fair Value Application in Czech Accounting Rules

not	55	14.8%
yes, for reliably measured items only	293	79.0%
yes, without any limitation	23	6.2%

During last thirty years there is visible a wider spread of fair value measurement in international accounting practices (US GAAP, IFRS). Since 2013 this measurement base has its own international standard, concretely IFRS 13 with its famous fair value hierarchy. Fair value is a useful measurement base in case we are applying it on transparent and active market, however it is a discussable issue whether (and how) to use this measurement base in emerging markets.

The results of this survey show that respondents are for fair value measurement just in case it would be reliably measured. When we asked respondents on their own view on fair value measurement their reactions were in line with these two selected ones:

- *I'm for the applying of fair value only in case that there exists for the asset/or liability active market. I'm for the elimination of the qualified estimation (Level 3) – in such a case there shall be rather preferred historical cost.*
- *Fair value accounting has a general problem in case, that the fair value is not objectively measured. Fair value shall be used “prudently” in financial statements and this value has to be really reliable and objective. From this point of view I rather prefer historical costs accounting with impairment tests.*

6 – Obligatory Financial Statements

balance sheet	364	98.1%
income statement	358	96.5%
statement of comprehensive income	62	16.7%
notes	264	71.2%
cash flow statement	131	35.3%
statement of changes in equity	161	43.4%

According to current Czech accounting legislature, obligatory parts of financial statements are: (i) balance sheet, (ii) income statement, and (iii) notes. Facultative parts of financial statements are: (i) statement of cash flows, and (ii) statement of changes in equity. Under international rules (IFRS) all parts of financial statements are obligatory, however income statement was replaced by statement of comprehensive income (and balance sheet is officially named statement of financial position). Based on the results respondents prefer current Czech status quo, i.e. just balance sheet, income statement and notes obligatory parts of financial statement. What is quite interesting finding, after in-depth analysis, this trend is more visible for IFRS companies rather than for other.

7 – Major User of Financial Statements

owner	223	60.1%
potential investor	5	1.4%
creditor	95	25.6%
tax authority	48	12.9%

Obviously, the target user for continental financial reporting systems, is owner, however for IFRS rather the potential investor. Based on the results of this survey, owners and creditors significantly dominated. Potential investor could be seen here just as a marginal user. The reasoning might be a fact that majority of companies do not issue bonds or shares which are publicly traded.

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4 QUESTIONS THAT MUST BE ANSWERED WHEN CONSIDERING IFRS IN CZECH SMALL AND MEDIUM SIZED ENTERPRISES

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Abstract: *In this article the author introduces 4 questions that must be answered by management of Czech small and medium sized enterprises when considering IFRS. First of all it is needed to know what IFRS represents, what are the main features of IFRS, what is the difference between IFRS, IFRS for SMEs and Czech accounting legislation (WHAT?). Secondly the management shall answer what are the reasons for the use of IFRS (WHY?). Thirdly it must be decided how the IFRS can be used, if the small and medium sized enterprise will prepare financial statements under IFRS and what instruments can be used for possible adoption of IFRS (HOW?). And last but not least the impact of IFRS on the company, its personnel and processes shall be considered (IMPACT?).*

Keywords: *Czech Republic, IFRS, small and medium sized enterprises*

1. INTRODUCTION

IFRS as global rules for financial reporting is something what has been discussed by accounting professional and academics for many years, however what is still being very little used in a real world of Czech small and medium-sized enterprises.

If we ask typical representatives of Czech small and medium-sized enterprises why they prepare financial statements and what information they present in their financial statements they usually reply that they prepare them because they have to as it is required by accounting and tax legislation and that they tend to show as minimum information as possible. This attitude to financial reporting is very far from the main ideas of the prepares and promoters of IFRS.

Based on the literature review the author of this article assumes that if Czech small and medium-sized enterprises would change their attitude to financial reporting and would be able to prepare high-quality, transparent and comparable financial information, this would help them to overcome their typical weaknesses like the lack of capital, higher cost of capital available and complications in obtaining bank loans.

It is undisputable that the adoption of IFRS by the company brings benefits to the users of financial information as well as to the company, however the costs connected to this change are significant. The decision about the IFRS adoption therefore has to be done very properly and the management shall be able to answer following questions when considering IFRS adoption.

2. WHAT?

First of all the management has to have the idea what IFRS represents. To answer this question an official web pages of IFRS Foundation www.ifrs.org can be used. The readers can found following information there, “*IFRS represent a single set of high quality, understandable, enforceable and globally accepted standards developed by IASB, the independent standard-setting body of the IFRS Foundation. The principal objectives of the IFRS Foundation besides the development of the IFRS, is to promote the use and rigorous application of IFRS, to take*

account of the financial reporting needs of emerging economies and small and medium-sized entities and to promote and facilitate adoption of IFRSs, being the standards and interpretations issued by the IASB, through the convergence of national accounting standards and IFRSs.” (IFRS Foundation, 2013).

Up to 2000, IFRS were only supported by professional organizations. In 2000, the European Commission announced IFRS as a regulatory tool for the European accounting. Subsequently in 2004, the requirement that companies listed on a regulated market in the Member States of the European Union, were required to prepare their consolidated financial statements under IFRS came into force. Since 2005 Czech companies whose securities trade in a regulated securities market prepare their consolidated financial statements under IFRS. The Czech Republic has also permitted companies whose securities do not trade in a public market to use IFRS when preparing the consolidated financial statements, as well as IFRS are permitted in the separate company financial statements of a company whose securities do not trade in a public market if it is a subsidiary of a parent company that uses IFRS for preparation of its consolidated financial statements. Those companies who decide to prepare their individual financial statements under IFRS are obliged to prepare the conversion of the IFRS financial result to the financial result under Czech accounting rules in order to set the tax base for the corporate income tax. The fact that tax base cannot be calculated from IFRS financial result is the key limitation of widespread of the usage of IFRS in the Czech Republic. Companies usually need to keep two sets of accounting to be able to calculate the tax base and corporate income tax which increases the costs.

In the above mentioned IFRS represent full IFRS used mainly for listed companies. In addition to full IFRS the IASB has published an IFRS for SMEs in July 2009. The objective of this project running since 2003 was to develop an IFRS expressly designed to meet the financial reporting needs of small and medium-sized entities that do not prepare their financial statements for the needs of equity investors in companies in public capital market but they are more focused on assessing shorter-term cash flows, liquidity and solvency instead. In June 2013 the European Commission examined and rejected the option to adopt the IFRS for SMEs at EU level. The Impact Assessment concluded that introducing the IFRS for SMEs would not appropriately serve the objectives of simplification and reduction of administrative burden. For instance, the Directive does not require preparation of a cash flow statement, whereas this is mandatory under the IFRS for SMEs. Nevertheless, Member States are able to permit or require the IFRS for SMEs as their accounting standard for all or some of their unlisted companies (European Union, 2013). The Czech Republic has not adopted the IFRSs for SMEs and the adoption is not under consideration in the nearly future.

When considering IFRS, it has to be decided if the company would adopt full IFRS or IFRS for SMEs. When introduced, IFRS for SMEs, were expected to widespread very soon, however in developed world IFRS for SMEs is still being used very rare when compared to developing countries who have adopted IFRS for SMEs instead of creating their own accounting legislation. Majority of Czech companies who decide to prepare their financial statements under IFRS use full IFRS even though they are more complex.

3. OVERVIEW OF DIFFERENCES BETWEEN IFRS AND CZECH ACCOUNTING LEGISLATION

When considering IFRS the management has to be aware about the differences between Czech accounting legislation and IFRS. According to EY (2010) the differences can be divided into conceptual differences and specific differences.

Conceptual differences:

- CZ GAAP is based on rules but IFRS generally on principles.
- Czech tax base is still based on Czech accounting legislation. Consequently, a lot of the assumptions the management makes during the preparation of the financial statements is made with the potential tax consequences on that accounting treatment. This could (and often results) in adoption of the tax-founded point-of-view in accounting rather than of a real consideration what is the true and fair view of the transaction in its substance.
- CZ GAAP, again due to its nature, does not have a thorough conceptual framework that would describe the following:
 - the individual elements of the financial statements and their definition,
 - the conceptual discussion about the fundamental accounting concepts and methods on which the financial statements should be prepared,
 - assumptions behind the quality of neither information that the financial statements should provide not a hierarchy referring to other legislation's or accounting literature in case of non-existence of relevant rules. (EY, 2010)

List of significant specific differences:

- Financial statements
- Revenue recognition
- Borrowing costs
- Fixed assets valuation
- Recognition criteria for long-term assets
- Assets held for sale
- Investment property
- Amortization of goodwill
- Financial lease
- Grants accounting
- Provisions recognition
- Extraordinary items
- Impairment rules

To understand the specific differences it is needed to have basic knowledge of IFRS, many publications comparing IFRS and Czech accounting legislation are available online (e.g. on web pages of big 4 audit companies www.pwc.com/cz, www.ey.com etc.).

4. WHY?

To answer why the usage of IFRS could be beneficial for the company some points from recent academic studies can be mentioned.

According to Mirza, Orrel, and Holt, the adoption of standards that require high-quality, transparent and comparable information is welcomed by investors, creditors, financial analysts and other users of financial statements. Without common standards, it is difficult to compare financial information prepared by entities located in different parts of the world (Mirza, Orrell, Holt, 2008). Gassen and Sellhorn based on German data from 1998–2004, reported that company size, internationalization of business activities and dispersed ownership were positively related to the voluntary adoption of the IFRS. They also state that the quality of IFRS financial statements is higher than those based on local accounting standards due to decreased information asymmetry (Gassen, Sellholm, 2010).

Soderstrom, and Sum say that implementation of the IFRS should bring improvements in the quality of the reported information, even if it is not assumed, that information will significantly differ under the application of IFRS. The quality of the reported information is

besides different accounting rules also influenced by legal and political system in every country as well as different requirements on reported data (Soderstrom, Sun, 2007).

A study of Paglietti, that compares the quality of financial information prepared according to IFRS and according to the Italian legislation, shows that in all areas the data according to IFRS are of better quality. This study also compared the improvement of the quality of the financial information in the services sector and for production companies and it was found that the information prepared by production companies have been more consistent in both accounting legislations (Paglietti, 2009).

In 2009 Hellström presented a study that compared the data that must be compulsory reported under IFRS and Czech accounting legislation at the Congress of EAA in Tampere. In 2001, Czech accounting legislation required data in 21 areas to be presented, under IFRS there were information in 15 more areas to be presented. Hellström also states that good enterprises have a tendency to disclose additional information on a voluntary basis or they prepare additional financial statements under IFRS if they believe that it will bring them some benefits, such as new investors (Hellström, 2009).

This was also confirmed by the survey carried out by PricewaterhouseCoopers (PWC), when 187 investors confirmed that the ability to submit reports in accordance with IFRS is of great importance and impact on their investment decisions. Investors said that improved transparency and better management information, as well as consistency in reporting between countries and sectors are the major benefits of reporting according to IFRS (PWC, 2010).

To sum up, the financial statements prepared in accordance with IFRS (both full IFRS as well as IFRS for SMEs) are considered to give better information to the users of financial statements than financial statements prepared under Czech accounting legislation mainly because of their better understandability and comparability, as well as due to the amount of information, that must be disclosed in the financial statements. Because of these facts application of IFRS can bring to Czech companies following opportunities – the companies have more accurate information about financial position of the company, they have increased possibilities of financing and finally they can have better relationship with their stakeholders.

5. HOW?

One of the drawbacks of IFRS adoption in the Czech Republic is the complexity of full IFRS as well as lack of professionals with significant knowledge. Adoption of IFRS for SMEs is easier than application of full IFRS however the steps of the implementation process shall not differ.

According to Jermakowicz and Gornik-Tomaszewski implementation of IFRS brings not only a change in format of financial statements, accounting policies, and much more detailed reporting information, but also great changes in company that IFRS implements. These changes require financial costs and the human resources and they may take up to 24 months before implementation is ready. A lot of organizations are struggling with a lack of high-quality staff with IFRS knowledge, also IT changes are very significant, because it's not just about the changes in the accounting system, but mostly it requires the creation of a new accounting system besides an existing accounts used for the statutory purposes (Jermakowicz, Gornik-Tomaszewski, 2005).

The increased costs of IFRS reporting are mainly represented by costs in the implementation phase, costs prior to the decision if the company will report under IFRS, and also the costs after implementation. The cost prior to the decision mainly include the cost of training and materials, so the company can understand the concept of IFRS. The implementation costs include the costs of changing the accounting software, accounting policies and processes in the enterprise. As reported by the consulting company PricewaterhouseCoopers, *important to ensure that implementation took place without problems is a major preparation for the transition and*

the "teaming" or constant communication across the Enterprise (PWC, 2010). Subsequent costs are mainly the costs of staff, which will prepare the reporting in accordance with IFRS.

Based on the experience of companies that have already implemented IFRS following steps have to be done in the implementation process, see Fig. 1.

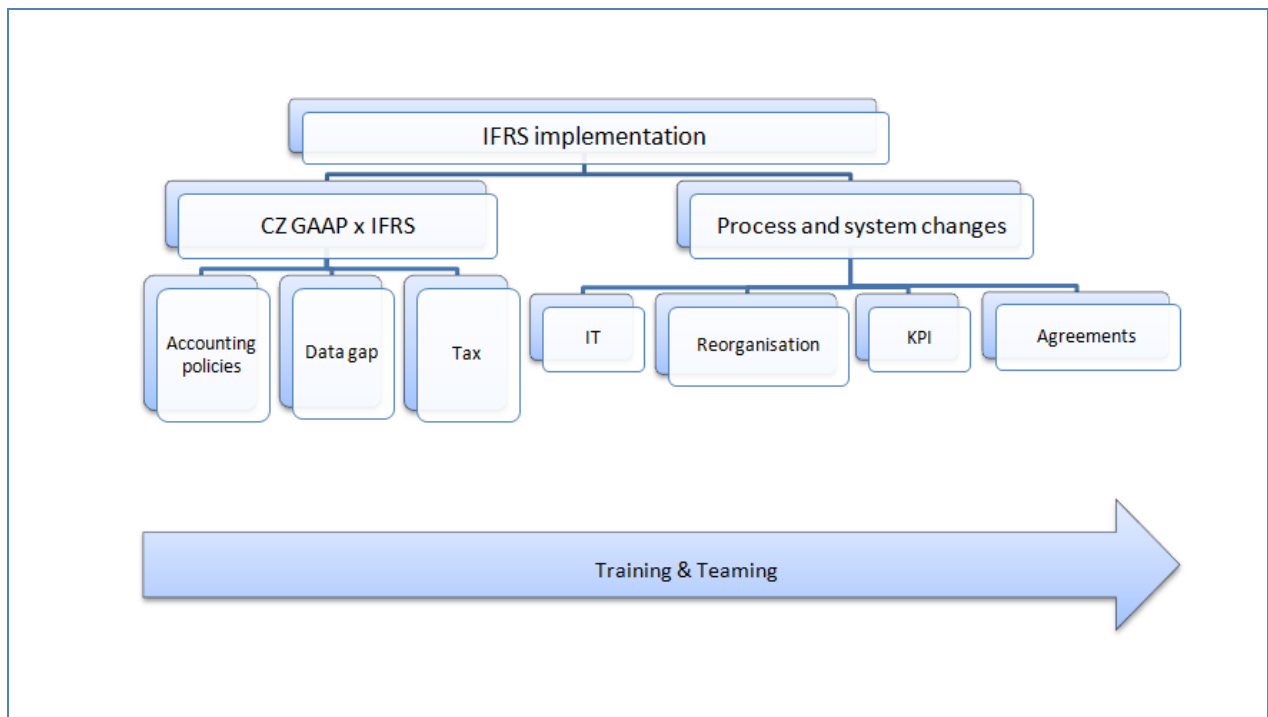


Fig. 1. Steps in the implementation process. Source: prepared by author based on PWC 2010

To begin with, it is necessary to understand the difference between Czech accounting legislation and IFRS. Based on these differences, the change of accounting policies is essential. Furthermore, it is necessary to improve data collection and eliminate data gaps because the disclosure requirements are wider for the IFRS. It is also recommended to consider tax implications.

Next step is the assessment of the process and system changes. The IFRS implementation will need the changes IT – upgrade of accounting and information system, change of connected systems (e.g. systems used for the revenue recognition). With the changes within IT and the accounting policies the companies may use the synergy effect and the business processes can be reorganized. In line with all these changes the KPI used in the organization can be affected. Also some internal and external key agreements may be reviewed and changed in accordance with their substance.

During the whole process training and teaming is significant. Training is important for accountants to perform their job but also for other employees to understand the changes in the company. The good implementation team shall ensure that the implementation is performed with minimum constraints and problems.

The above mentioned is the best practice what the company can use when adopting IFRS, it is however most costly and requires sufficient sources, both financial as well as personnel. Many companies willing to adopt IFRS will start with simple spreadsheets where using a bridge they will transform their financial data from Czech accounting into IFRS. The bridge shall automatically perform reclassifications to change balance sheet and income statement format under Czech accounting rules to financial statements under IFRS. The adjustments calculated due to different accounting principles have to be added into the bridge manually. The bridge shall include check cells to ensure that the adjustments were added completely. They will also need to prepare and collect additional data needed for the preparation of Cash flow and the Notes to the financial statements. This option is however not very systematic and needs frequent

changes into spreadsheets which can result in errors during the process of preparation of financial statements under IFRS.

If the company decide to adopt IFRS full compliance is recommended, that means that the company is able to present its financial statements with Notes. Many Czech companies usually those who are part of foreign group decide not to prepare complete set of financial statements under IFRS but only to prepare data needed by Group. They usually perform some transition of Czech financial statements into financial information to be filled into reporting packages. This is the less costly variant however the company is not able to present its IFRS financial data to other users than to the group.

6. IMPACT?

As it was mentioned above, the IFRS adoption will bring not only changes in the accounting system of the company but also the changes in IT and processes. The company shall spend sufficient time to prepare the IFRS adoption and to go through all steps in the process of implementation. This will then ensure that the implementation was sufficient and that the data presented in IFRS financial statements are correct.

The users of the financial data (both external as well as internal) shall profit from the more accurate financial data, however it has to be noted, that the interpretation of data prepared under Czech accounting legislation and IFRS will differ in many areas.

If the company uses the reporting packages the whole system of reporting the company performance will have to be adjusted. The packages have to be prepared in accordance with the data available from the Financial Reporting. The structure shall be adjusted to the new format of Financial Statements as well to better data availability. Due to the change in the reporting packages training has to be provided to the fillers of the reporting packages.

The Financial Manager shall also update the evaluating tools and has to distinguish the effect of the Financial Reporting system change from the effect of the units operations.

The performance of the units reported in the reporting packages is usually one of the factors in the evaluation of managers and as well it is used for the management decisions related to funds provided to individual units. It is necessary that the users of the information from the reporting packages have the knowledge of the effect of the shift in the Financial Reporting.

7. REASEARCH AT TOMAS BATA UNIVERSITY IN ZLÍN

As a part of the GA CR project No. 402/09/0225 “IAS/IFRS Usage in Small and Medium-sized Enterprises and its Influence on Performance Measurement” we have performed trial conversions of financial statements of Czech companies prepared under Czech accounting rules (CZ GAAP) into financial statements prepared in line with IFRS (both IFRS and IFRS for SMEs based on the decision of Companies).

The data used for the conversion were the financial statements for the year ended 31.12.2008 and detailed data provided by accountants and financial managers of these companies. No changes were made in the companies’ accounting systems as well as no opening balance sheet was prepared, only closing balances were transferred. In case of adjustments that should have been done in prior accounting periods retained earnings were adjusted to ensure that equity as at 31.12.2008 is correct. Full set of financial statements were not prepared as well as the disclosure. The companies were only informed about the requirements and had training how to prepare the full set of financial statements.

The adoption had following phases:

1. Analysis of the financial statements prepared under CZ GAAP and evaluation of current accounting policies applied in the companies
2. Identification of financial statements areas where different approach is used under CZ GAAP and IFRS
3. Calculation of adjustments needed for the preparation of financial statements under IFRS
4. Preparation of financial statements under IFRS using bridge
5. Financial analysis of both sets of financial statements and the evaluation of the accuracy of information provided in the financial statements
6. Evaluation of the process of the trial conversion and recommendation in case of real adoption
7. Discussion with the representatives of companies why of why not has the company intention to adopt IFRS after the experience with the trial conversion

In Fig. 2 it can be seen how the conversion affected EBT and total assets – increase of EBT by 78% companies and increase of total assets by 56% companies.

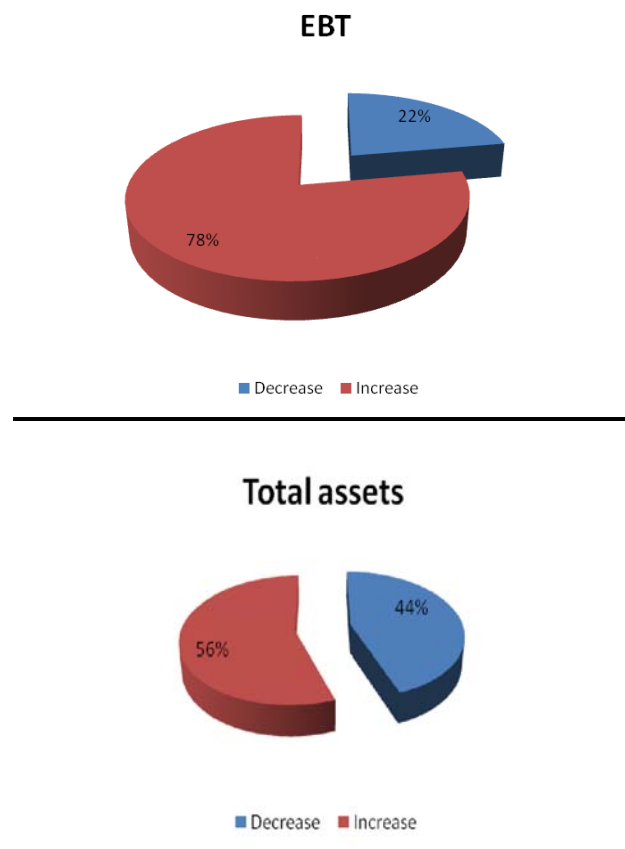


Fig. 2 Effect of trial conversions from CZ GAAP to IFRS on EBT and total assets.
Source: own analysis

In Table 1 it can be seen how the individual categories of financial statements has changed – if it has increased, decreased or if there was no change.

Table 1. Effect of trial conversions from CZ GAAP to IFRS

	Decrease	Increase	No change	Note
ASSETS				
Long-term intangible assets	0%	44%	56%	B
Long-term tangible assets	11%	78%	11%	A
Activation of low value assets	0%	89%	11%	B
Long-term financial assets	11%	11%	78%	E
Long-term receivables	0%	33%	67%	F
Inventory	22%	11%	67%	B
Short-term receivables	22%	56%	22%	F
Allowance to receivables	0%	22%	78%	C
Short-term financial assets	0%	11%	89%	E

	Decrease	Increase	No change	Note
LIABILITIES				
Retained earnings	22%	56%	22%	A, B, D
Provisions	33%	33%	33%	C
Long-term payables	0%	56%	44%	A
Short-term payables	0%	89%	11%	A
Loan	11%	0%	89%	E

	Decrease	Increase	No change	Note
PROFIT AND LOSS				
Activation	22%	0%	78%	D
Operating expenses	67%	0%	33%	B
Services	56%	0%	44%	A
Depreciation	0%	100%	0%	A, B
Change of provisions and allowances	22%	44%	33%	C
Other operating revenues	11%	44%	44%	D
Interest expense	0%	67%	33%	A
Revenues	11%	0%	89%	E
Interest income	0%	11%	89%	E
Extraordinary revenues	33%	0%	67%	D
Extraordinary expenses	33%	0%	67%	D

Source: own analysis

Note A: Significant increase of tangible assets and payables (both short-term and long-term) was mainly due to effect of leasing adjustment. Connected to activation of leased assets the depreciation has increased. The services have decreased due to the elimination of lease costs booked under CZ GAAP. The Interest expense has increased due to the recognition of lease. This adjustment was performed in 78% of all companies.

Note B: Effect of activation of low value assets (booked in CZ GAAP in operating expenses) and transfer of some items booked in CZ GAAP in inventory but meeting the criteria of tangible assets. The depreciation increase is also affected by this type of adjustments. This adjustment was performed in 89% of all companies.

From notes A and B it can be seen that leasing adjustment and activation of assets are frequently used adjustments and represent the most frequent differences between IFRS and CZ GAAP.

Note C: Here we can see the frequency of other quite often in literature mentioned differences which are provisions and allowances. In our research it can be seen that the provisions which are booked under CZ GAAP but do not meet the criteria of provision under IFRS are not so often

present (only by 33% of companies). On the other hand in some cases there have been some provisions in CZ GAAP missing (also by 33% of companies) and they had to be created for IFRS. By 22% of companies additions allowances to receivables have been created in line with IFRS.

Note D: Here we can see the reclassification that was needed because of extraordinary items used in CZ GAAP but not allowed under IFRS, this was a case of 33% of companies and has been reclassified according to the type into other expenses or revenues or into retained earnings. The other case is the case of activation which was used by 22% of companies and which had to be reclassified from revenues into costs to be in line with IFRS.

Note E: This represents the items in the financial statements with not significant change. Quite surprisingly are also revenues represented in this category when by 89% of the companies there were no changes.

Note F: The increase of receivables can be explained by the reclassification of deferred assets which are under CZ GAAP recorded as a separate item of financial statements.

From this research it is obvious that the IFRS adoption will have impact on financial analysis, there are no rules that can be applied generally, the movements differ from company to company and depend on the actual corrections needed for transfer of CZ GAAP to IFRS. However it can be outlined what ratios are affected by individual corrections (it is assumed that the company has adopted IFRS for SMEs), see Table 2.

Table 2. Effect of CZ GAAP x IFRS for SMEs differences on selected ratios

Differences	ROS	ROA	ROE	Current ratio	Debt/equity	EPS
Revenue recognition	X	X	X		X	X
Borrowing costs	X	X	X		X	X
Fixed assets valuation	X	X	X		X	X
Recognition criteria for long-term assets	X	X	X	X	X	X
Assets held for sale	X	X	X	X	X	X
Amortization of goodwill	X	X	X		X	X
Financial lease	X	X	X	X	X	X
Grants accounting	X	X	X		X	X
Provisions	X	X	X	X	X	X
Extraordinary items	X	X	X		X	X
Impairment rules	X	X	X	X	X	X
Reclassification	X					

Source: own analysis

As it can be seen all selected ratios are affected by more than one adjustment to be performed when adopting IFRS and it always depends on the materiality of individual differences and on the fact which difference prevails. The result of financial analysis can therefore be favourable for one company whereas very unfavourable for other. In both cases it is assumed that based on the principles of IFRS financial analysis prepared under IFRS can give better information about the financial situation of the company.

To illustrate this I have chosen 3 companies from trial conversions performed. Company A is a micro-company and is part of foreign group which has its operations in Europe as well as United states. Company A is a production company. Company B is a medium production company with cross country operations and major sales abroad, it is owned by management,

research and development is crucial for the company. Currently Company B is implementing new information and reporting system. Company B is a typical “born global or international” as classified by (Ikäheimo, Ojala, Stening, Riistama, 2010). Company C is small company with operations only in the Czech Republic having monopoly in the region where it provides services. It is owned partly by management and partly by external entities and individuals. Company A prepares financial statements under CZ GAAP only to meet the requirements of Czech accounting and tax legislation. The financial statements are prepared in short format (do not include cash flow statement and statement of changes in equity). Also deferred tax is not calculated. The accounting policies are in line with the group accounting policies based on IFRS where possible. For the management decisions data from group reporting are used. Company B uses financial statements prepared under CZ GAAP as well as for statutory purposes also for management decisions. Company B is currently changing the reporting system and implementing new information system to improve the information used for decision making. This is due to the fact that the company has grown in past years and it has to build new processes for the managing the company. It prepares full set of financial statements and the accounting policies are currently being reviewed within the implementation of new systems. Company C prepares also full set of financial statements and has already information and reporting system implemented that provide sufficient data for the company management. The company has no intention to grow or to extend the services provided. All companies decided to prepare trial financial statements under IFRS for SMEs. In Table 3 Areas with different approach under CZ GAAP and IFRS in these 3 companies can be seen.

Table 3. Areas with different approach under CZ GAAP and IFRS

	Company A	Company B	Company C
Financial lease	X		X
Fixed assets	X	X	X
Inventory		X	X
Provisions		X	X
Deferred tax	X	X	X
Revenue recognition		X	X
Extraordinary items	X	X	
Financial statements presentation	X	X	X

Source: own analysis

Adjustments for the areas of difference stated in Table 3 have been calculated using supporting data obtained from the companies as well as the information from the discussion with the accountants and management of the companies. The most complex adjustments were in the areas of financial lease and deferred tax. In the financial statements presentation in all three companies reclassifications were needed to prepare the financial statements. Preparation of full set of financial statements in Company A would be more complex as in two remaining companies, as this company prepares only short version of financial statements under CZ GAAP. However mainly the preparations of notes under IFRS for SMEs is much more complex than preparation of notes under CZ GAAP and therefore the disclosure requirements have to be taken into account in all sample companies.

The results of financial analysis comparison are showed in Table 4. The conversion had positive effect on ROS by all three sample companies; debt/equity and current ratio had worsened by all three companies. Effect on ROA and ROE differs by sample companies. The most unfavourable result of financial analysis under IFRS for SMEs is for the Company C mainly due to the increase of debt/equity compared to debt/equity under CZ GAAP. For Company A and B the result is neutral as the change of ratios is not significant.

Table 4. Effect of conversion on selected ratios.

	(a)	(b)	(b) – (a)
	CZ GAAP	IFRS for SMEs	Diff.
Company A			
ROS	3,70%	3,78%	0,08%
ROA	14,00%	13,93%	-0,07%
ROE	17,00%	17,20%	0,20%
current ratio	2,7000	2,6000	-0,1000
Debt/equity	35,80%	35,97%	0,17%
Company B			
ROS	14,59%	15,46%	0,87%
ROA	11,67%	11,59%	-0,08%
ROE	15,64%	15,51%	-0,13%
current ratio	3,2444	3,2395	-0,0050
Debt/equity	26,05%	26,09%	0,04%
Company C			
ROS	5,50%	6,04%	0,54%
ROA	1,14%	1,24%	0,10%
ROE	0,88%	0,82%	-0,06%
current ratio	1,9000	1,2100	-0,6900
Debt/equity	16,88%	17,70%	0,82%

Source: own analysis.

After the evaluation of the process of trial conversion and recommendations to companies, discussion with the representatives of companies were held to see if these sample companies has intention to adopt IFRS for SMEs after the experience with the trial conversion. Reasons why and why not are summarised in Table 5.

Table 5. Reasons why/why not the sample companies' intent to adopt IFRS for SMEs after the experience with trial conversion.

	Company A	Company B	Company C
Why	<ul style="list-style-type: none"> Because of the requirement of mother company 	<ul style="list-style-type: none"> To provide understandable financial statements to stakeholders of the company, mainly foreign business partners Comparative advantage in EU grants Could help company in setting the reporting system and providing data more focused on management of the company, data more focused on substance over form than tax 	<ul style="list-style-type: none"> If forced by owners or legislation

Why not	<ul style="list-style-type: none"> • Czech tax legislation and related cost to prepare two sets of financial statements 	<ul style="list-style-type: none"> • Czech tax legislation and related cost to prepare two sets of financial statements • Not significant difference shown in financial analysis comparison 	<ul style="list-style-type: none"> • Czech tax legislation • No need to present financial statements under IFRS for SMEs, financial statements under CZ GAAP more favourable for the company • Cost related to IFRS for SMEs adoption
Intention to adopt IFRS for SMEs in nearly future	<ul style="list-style-type: none"> • May be forced by mother company to prepare IFRS financial statements in nearly future, allowance of IFRS for SMEs for statutory purposes would be appreciated 	<ul style="list-style-type: none"> • In case Czech legislation would allow IFRS for SMEs for statutory purposes use rather IFRS for SMEs than CZ GAAP, no intention to prepare financial statements under CZ GAAP and IFRS for SMEs 	<ul style="list-style-type: none"> • No intention to report under IFRS for SMEs if not required by law of owners

Source: own analysis.

CONCLUSION

In this paper answers to 4 questions that have to be answered when considering IFRS were mentioned. Firstly short overview of IFRS was provided, than based on the literature review the profits of IFRS adoption were stated. Furthermore the changes in company when it decides to adopt IFRS were recommended and the impact of IFRS adoption was illustrated using data from trial conversions performed at Tomas Bata University in Zlín in 2009.

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EXTRACTING ECONOMIC BENEFITS THROUGH LOCAL USE OF A GLOBAL FINANCIAL REPORTING INSTRUMENT – THE CASE OF ASSET WRITE-OFFS IN SLOVENIA

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Abstract: *In 2002, Slovenia has introduced new accounting standards (SAS, 2002). One of the defining features of these new standards was the explicit introduction of IFRS-like asset write-offs. The introduction of a new financial reporting instrument by the new standards was immediately seized by publicly-quoted firms to: i) get rid of “dead” assets that resulted from the privatisation process; and ii) to maximize the value of the tax shield resulting from a reduction of the tax base. However, it was also seized by private firms, many of them small, to manage earnings in a way that allowed them to maximize the value of the tax shield resulting from write-offs. This requires a close alignment of financial and tax reporting. In principle, write-offs (as well as the financial reporting process) are redundant if the manager and the owner is the same person as they are able to observe the true state of the firm regardless of write-offs. Observing this behaviour is not straightforward as firms weight the value of the tax shield against other tax and non-tax costs of reporting lower earnings via write-offs. Due to political costs of being exposed to a tax audit, firms in many instances reduce reported earnings to a level that is presumably viewed as “suspicious” (loss or zero earnings or relatively very small earnings). Contrary to predictions from standards, local research shows that more profitable companies are more likely to write-off assets and the amount of write-offs is higher, reflecting tax minimization. Larger companies are more likely to write-off, but the magnitude decreases with size, reflecting increasing political costs due to greater visibility to tax authorities. Previous write-off patterns and magnitudes are persistent, reflecting institutional learning linked to regulatory changes. Firms also respond to an exogenous change of economic incentives and adjust the financial reporting process accordingly. The same process happens if economic incentives are similar, but accounting standards are different. The main insight from this research is that the introduction of high-quality international accounting standards is not a sufficient condition for high-quality financial reporting, but that the institutional background is at least of equal importance, if not more important than accounting standards.*

Keywords: *political costs, Slovenia, tax minimization, tax shield, write-offs*

UNDERSTANDING CORPORATE COSTS AND SUSTAINABILITY

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Abstract: *This material aspires to start to evaluate every sort of corporate cost. Costs from the view of modern corporation. Traditionally there are material cost together with depreciation, salary cost and personal cost, financial cost and other cost. For managerial purposes we distinguish between standard and nonstandard cost. Special attention is devoted to responsibility costing and division of costs. In this modern age, however it is a question whether our understanding of cost should be so narrow and limiting to money that a corporation spends during the course of its production, or whether it should include also the costs of negative externalities – the damage the company causes to the environment. Therefore the final part of this contribution deals with function of cost and attempts to provide an evaluation of basic sorts of cost in modern corporation from a broader more societal perspective*

Keywords: *sort of cost, depreciation, financial cost, division of responsibility cost, evaluation of cost, effectiveness of the process, externalities.*

1. CORPORATE COSTS AND ITS BASIC STRUCTURE

The general definition of cost can be considered as: “Sacrifice of scarce resources.”

It is possible, of course, be understood by their users as their concept works as follows:

- Costs recognized in the financial accounting, or pumping of equity, are not only the means or necessarily incurred in securing reproductive state, but all expenses, including entertainment, taxes and fees; In even broader sense, the construction of production should include not only the costs of production and services that the business uses in the course of production, but it should also include that costs of damage the company cause to the environment.

Furthermore the tax costs are broken down by tax law to:

- Tax deductible – reducing the tax base,
 - Tax deductible – are not reflected in the reduction of the tax base;
- Costs in terms of management, for which managers consider reasonably incurred sources of economic growth (property), assigned to the implementation of related objects of the undertaking. And continue a bit on the environmental view.
 - Who is responsible for the destruction of the environment – society – modern theories of CSR or would it be all correct by government of state and the company only pays taxes?
 - And what about the social morality of the corporation and its management? For example, I pointed to this topic sure contradiction recently in policy bank. When favorable legislation regarding the construction of solar power plants, the mathematical return of loans based on very well, the bank fell on this type of business rapidly. Banks promote the construction of solar power plants on fertile agricultural land and even in areas of weak sunshine. Once the legislation has changed as rapidly these banks have ceased support for such projects.
 - Justification that it is a renewable and future environmental decision-making should not weight for banks. Currently, we see support banks for the construction of biogas plants, because these have now support the European Union.

- The example banks, we see that often still have a major economic impact numbers than the sight of the future manager of the Earth.
- We can proposed to make ethical behavior part of the firm’s culture, leadership, teamwork and people management in general.
- The basic breakdown of costs.

Most often we divide the cost according to the following aspects:

- Generic
- Purpose
- Calculation
- Power costs – in relation to production volume
- According to their place of origin a responsibility for them.

Expenses according to their types distinguished as:

- Material costs, including depreciation
- Payroll and other personnel costs
- The financial costs
- Other expenses

Zoning costs distinguished as:

- Unit costs
- Overheads

Calculation broken distinguishes costs as costs:

- Direct – associated with one type of performance
- Indirect – cannot be directly assigned to individual performance. They are particularly critical component of overhead costs and therefore often confused with them.

We divide the costs of power:

- Variable – tied to the volume of production (output)
- Fixed – usually the change is abrupt and is associated with exceeding the limits of each production. In the long run, we can evaluate it as a variable.

Places of costs and responsibility for their creation:

- Economic centers – can be defined as the higher body types of economic structure, which measured their costs and benefits quantified and its profit.
- Cost centers – the lower type of economic structure, which follows the planned costs and real.

The view of the cost, than only a limited view of current accounting rules and commonly used in managerial practice. The concept of cost should not be limited to management concepts to maximize profits and the value of the corporation, but there should be a broader concept outgoing from the stakeholder theory. Although, there is a practical problem with the bill. But it is important to keep the view from the perspective of sustainability.

We can see different approaches are through the Full Cost Accounting or Life cycle accounting, tracing the development of the company during its life cycle, and thereby also dynamically changing nature of the relevant costs that the company is considering. Currently it is not practical methods, because in practical application it is rather a problem of management accounting – or the problem of internal accounting each corporation.

1.1 Responsibility centers

The following structure of the centers can in principle be applied to any business.

Cost Center (cost centers) – the lowest department to which they are established budgets controllable costs and compare budgeted and actual costs. The bank is the centers responsible for the implementation of services, which cannot reliably determine which other banking services, these services were provided. (e.g. Marketing, Human Resources, etc.)

The Profit Center (profit center's) – generally it is the departments, whose leaders have the opportunity to influence factors affecting the costs and benefits – profit centers. The bank is the units responsible for the implementation of net profits – those foreign arbitration, securities trading, etc.

Profitable centers – not only responsible for the costs and benefits, but also the amount of funds that are tied to their activity.

Investment Centre (Investment center's) – have similar status as a profitable center. The bank is the departments responsible for implementation of profits related to amounts invested – especially to subsidiaries.

Yield (revenue) center (center's revenue) – analogous to a cost center with the possibility to influence the growth of revenues. The bank is the units responsible for the increase of certain income – for example, sales of electronic banking, credit cards, etc.

Spending center – responsible for expenses (no cost) – the aim is to control spending and sub-tasks. Service center (service center's) – those responsible for implementation of service to other departments. For example, the bank credit departments of administrative services.

PRODUCTION AND COST FUNCTION

The primary inputs in banks, as in all societies, are:

- Labor (L)
- Capital (K)

Their output is then output (Q).

On this basis we can then write the basic production function of the form:

$$Q = f(L, K)$$

Of course, it is necessary to consider the level of management control how the output changes in relation to inputs. Will output be the same percentage as input? It can be expressed algebraically as follows:

$$F(AL, AK) = n(Q)$$

Where:

And – which grows with constant inputs

n – exponent of homogeneity of the production function if:

n = 1 this is a linear production function with constant returns to scale

n > 1 the production function has increasing returns to scale

n < 1 production function has decreasing returns to scale

Economies of Scale

This is a savings associated with the scale of production, where the average (unit) production costs reduced in accordance with both inputs is increased. At the same applies if:

- Economies of scale ratio less than one, then there are economies of scale;
- Economies of scale ratio equal to or greater than one, then there are no economies of scale or diseconomies of scale exist.

Economies of Scope

These savings exist if the cost associated production of several products (goods, services) is lower than production costs from individual to individual products. If no, then it is preferable to implement each output separately.

These savings are in bank considered one of the most important; because banks always provide more than one product (multi-product company) and have considerable potential as achieve economies of scope – the most significant cost savings are reflected in the information systems.

2. SUSTAINABLE DEVELOPMENT AND THE ROLE OF BUSINESS IN SOCIETY

The concept of sustainable development is emerging in the literature about 60 years of the 20th century. It is inspired now several directions: economics, sociology, political economy and social philosophy, theory organization, organizational behavior and the consequences of population growth. At a meeting of the Club of Rome in 1968 was identified 11 critical areas for development humanity and sustainable population growth. From the limited mineral resources through the globalization problems of security, technology, education and development. The main aim of the report *The Limits to Growth* was not accurate forecast of development, but the effort to explore how the exponential growth of the world population cope with limited mineral resources.

The report describes the limits in different areas, because in 70 years have not yet been revealed additional reserves minerals and energy.

Another report from 2001 entitled *A New Way World Development*. It was written after the discovery of additional mineral reserves. It discusses more about the current population issues such as the environment and natural resources, globalization, international relations, social transformation and peace and security.

The world capital today is organized so that large enterprises in organizing social life of their capital strength. The financial capital of many large industrial and financial companies is larger than the budgets of entire countries.

This is therefore a very significant change in the status and role of business in society and change their decision-making power and ability to influence social events.

3. THE ROLE OF MANAGEMENT CONTROL

Management control is the process by which business entities ensure efficient use of resources to achieve their goals.

It is important to ensure the feedback control, which significantly improves the operation of management control.

The process of managerial control, we can define as follows:

- a) First Determination of the base. We start from both targets taken from plans and budgets, we can extend the results of the units and comparison with results of other units (benchmarking).
- b) Second Evaluation system resource consumption, especially information on the direct costs of the units, which can be attributed responsibility for them.
- c) Third the system evaluation results. In conjunction with the market, it is not difficult, but the problem arises in assessing the internal price at which it is appropriate to establish billing rates and possibly to compare prices on the open market.
- d) Fourth Comparison of the comparative base – variance analysis and explanation of their causes. Feedback can then react to changes in the environment. The reaction can then be divided into three levels of response:
 1. Degree of organization of the control unit – the feedback accelerates the realization of short-term and medium-term changes to achieve the objectives (the organization flows,

- tasks, rearrangement of resources, assigning responsibilities, changes in activities, products, services or clients, etc.);
2. Analysis helps improve planning and budgeting in the annual report;
 3. Analysis of long-term periods of time involved in preparing the reinvestment of resources across activities

The big question is whether management can look at the process control issues from the perspective of sustainable development and the future of the environment. Instruments managerial control described above is achieved by using the tools of management control.

For each tool we consider management controls:

Analysis and strategic planning – within the top management staff, such as CEO. Its aim is to determine the other directions of development, composition and the structural changes.

Strategic analysis leads to the initial setting medium-term goals are translated into well-defined and quantified targets.

Feedback as a strategic control then provides a recap of how to successfully achieve their goals.

Management control – the function equivalent credentials and has several components:

- Design Resources
- Coordination of resource allocation
- Organizing, recording and providing information

Operational management – the most important level of utilization management controls – is carried out specific activities and decisions are implemented. For example, reached the profit margin in continuously monitored both revenue (volume, price and distribution centers on responsibility) and costs (prices, productivity, utilization of skills).

Managerial control requires in principle the use of technical and organizational tools, in particular:

- Introduction of analytical accounting or cost management including tools and methods for assessing yields;
- Information system for the circulation and dissemination of management information;
- The structure defined responsibility centers as the main objects of management control.
- In this structure each center should have just had enough and the area of environmental accounting and sustainability.

4. ENVIRONMENTAL AND SUSTAINABLE DEVELOPMENT

The term corporate ethics is usually understood as a system of rather stiff rules and regulations by which the company manages itself and which it then proudly announces to the outside world in its annual reports in a hope to attract attention of new customers and possible investors in order to raise its sales and improve profits. We approach ethics in corporation as a discipline with practical and measurable outputs. And we suggest to measure the goals and progress achieved can be similar as in achieved progress through the key performance indicators, and apply the similar way as in general management and strategy building and control systems becomes more transparent. Further development of cooperation calls for deepening corporate culture which is based on responsible management between cooperating companies. This needs to be realized in the field of their innovative activities, in the field of strategy and development and managed subjects. In the opposite case the lack of deepening of cooperation within the country and internationally could negatively influence both business and political environments.

Issues of corporate governance are narrowly linked with corporation's ethics. This is apparent mainly in the view of recent corporate scandals around the world. We need to stress here,

that corporate governance and ethics are closely related fields and ethics or ethical behaviour needs to be understood as necessary precursor of good corporate governance (Jindrichovska, 2011).

Ethics comes first. It is a prevention measure, not a cure for consequences of bad behaviour.

Recommendations and important decisions must be based on expert opinion and investigation of the nature of the problem. The road to acceptance of the stakeholder management inspires today's academics and practitioners to pursue innovations of current management practices (Dytrt, Stříteská, 2009). Corporations need to be viewed as open systems, in contrast to shareholder management which manages corporations as separate entities. The struggle for ethical and responsible management is only at its onset. It entails primarily a wider complexity of management, which would be able to measure not only quantifiable outputs using norms and physical standards but it should also extend the measurement to non quantitative features. It needs to be stressed, that taking in consideration qualitative features of corporations extends the room for ethical behaviour and decent attitudes in management. Greater involvement of ethical management requires resolution the basic problems of management.

From the previous questionnaire research in the Czech Republic, where questionnaires were distributed to 2500 respondent, and the response rate was 18%, we have learned, that there are two key problems indicating, what is destroying ethical enterprising. The first finding confirms that there is not enough knowledge about usefulness and necessity of ethics in management. The second problem is caused by insufficient interest in innovating current managerial practices; i.e. manager relies on the past practices and this confines his/her future capacity and creativity. This contributes to deepening consumerism in management, basis of which is the non-ethical thinking in the society as a whole. (Dytrt, 2011).

Reliability and accountability in business practices help companies to compete on a fair basis. Unethical or outright illegal practices like for example corruption or slavery create an anarchic and completely unpredictable environment. This is why governments and also the EU try to introduce corporate governance procedures and processes, because an environment running wild will also damage the national / European economies in medium and long-term. The current crisis based on unethical while not illegal risk taking of the banking industry is a good example how unethical behavior and practices have the power of taking not only the EU down. We cannot get away from the complexity and interrelationships of globalization.

New dimensions of business in sustainable development

In connection with the concept of sustainable development is changing view of the enterprise, which is understood as a multi-dimensional unity of economic, social and environmental dimension. The reproduction of these dimensions allows its permanent (sustainable) development. Social and environmental dimensions of business closely related to the economic dimension. Not, however, say that the full implications of social and environmental performance of the company reflected in the reported performance of the company and its financial position. In accordance with the multi-dimensional view of the enterprise to form three lines of reporting - traditional economic dimension, which opens next communication space including also social and environmental aspects of business operations. Disclosure of social and environmental information is done through various documents and reports. These reports are compiled by a yearly basis, as well as financial statements.

Social and environmental factors may also be presented to the public as part of the output of financial accounting or reporting, usually as part of annual reports of the companies. The corporate can disclose social and environmental aspects in general either:

- a) in a separate report (reports), or
- b) in the annual report (or use both ways).

The information on the environmental and social impacts of activities business are presented in a variety of formats and range, most are not substantively comparable and often lacks continuity

with information on the economic dimension. Interactions have been demonstrated all dimensions of their business and need a complete, comprehensive reporting that will have the effect not only information, but will on the other hand, motivate businesses to environmental and social activities. Connection to Information Financial Accounting (where possible) and can also improve the quality and reliability such information.

Financial Accounting appears to be an appropriate tool for information sharing economic environmental and social dimensions of business.

Environmental and Social Reporting in the Czech Republic

The Ministry of the Environment of the Czech Republic defines its views on environmental and sustainability reporting as issues that are recognized on both microeconomic and macroeconomic levels. In 2005, the strategy of sustainable development was approved. The strategy combines environmental reporting with social issues into the so called system of sustainable development. With the use of this system, the state can assess the efficiency and material effects of legislative measures and voluntary measures used by individual companies and give recommendations that companies may use for assessment of sustainable development. “Reporting on sustainable development on the-enterprise level – i.e. the microeconomic level is a tool, which helps the decision-making of the company management. It seems very effective to connect the system of sustainable reporting with managerial accounting in the company, because they are both useful parts of communication with external bodies not only in the area of corporation approach to the environment but also in corporate annual reports and reports on corporation sustainable development. “The policy of the Ministry of Environment currently relies on voluntary corporate reports that deal mainly with health, safety and sustainable development of company; however, on the macroeconomic level the ministry defines accounting of sustainable development.

This consists of information on the current state of environment in connection with the economic performance of the state. On the company level, the reporting concentrates on fulfilling certain environmental goals. In our opinion the voluntary character of environmental reporting should remain, similarly as it is in other developed countries, and the Ministry of Environment should prepare recommendations and more detailed guidelines in accordance with the worldwide experience taking in consideration differences in industrial sectors. The Czech Ministry of Environment wants to include elements of sustainability reporting into mandatory company reports. One of the preferred tools for this reporting is Material Flow Cost Accounting, which was first developed in Germany and later modified in Japan. Material Flow Cost Accounting focused on cost reduction, having strived for significant productivity and environmental improvements through innovations in the manufacturing process.

At present, one of the most important activities in the area of environmental reporting is the enforcement of new ISO standards. In recent years, Japan initiated this activity, which served as a basis for successful commencement of works on the preparation of a new standard. Environmental costs represent all costs connected with environmental damage and protection. EMA (Environmental Management Accounting) is concerned with the accounting information needs of managers in relation to corporate activities that affect the environment as well as environment-related impacts on the corporation. The proposed standard Environmental Management – Material Flow Cost Accounting – General Principles and Framework is included in the group of ISO 14000 standards and has already been assigned with the denomination ISO 14051. In shaping the new standard, long discussion was dedicated to what is to be included in material flows. In spite of the fact that at first sight the methodology takes account only of material, material flow cost accounting includes also natural resources including water and also used energy. Discussions also included the types of businesses, which the methodology is intended for. Discussion has shown that new standard will give a number of impulses for future use of material flow cost accounting.

CONCLUSIONS

The global economic and financial crisis is still not completely overcome and the world economy and particularly the European economy are still different periods of the recession and no and no to have the better economic numbers. The companies are still in the big problem to increase performance and sales, from this perspective. The effectiveness of the all process in the company is very difficult to keep. The view of its internal management and the internal cost was significantly increased. From this point of view is very important to increase the level the control from the management as I write about it above.

The view on an enterprise is changing in connection with the adoption of sustainable development conception. An enterprise begins to be perceived as a unity of economic, social and environmental dimensions. A call for information about social and environmental dimensions of business is undoubted. This research positively validated that insufficient cohesion of information among economic, environmental and social dimensions of business weakens the information potential and reliability of presented information. On the contrary, the consistent use of multidimensional conception demands the information on all the three dimensions in an annual report. It opens a scope for new information quality which allows higher information potential of enterprise's annual reports as a whole, higher comparability of information in time and among enterprises, and also higher reliability.

We can say, hopefully, with optimism today, that large corporations are accountable and aware of their impact on the environment and those in charge want to take their share of responsibility.

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Summary and Final Comments

At the birth of the idea to organize a conference “**IFRS – global rules and local use**” was the desire and the need to bring together experts in accounting theory and accounting practice as well as academic and student community to enable the exchange of ideas and experience from the application of international financial reporting standards (IFRS) in specific national conditions.

Special attention was given to the influence of national cultural specifics of the process of implementing IFRS, its forms and results. Accepted and presented contributions bring characterize the current state of knowledge about application of IFRS at different levels and from different aspects

In summary, these contributions provide an interesting insight into the knowledge and experience brought about by the implementation of IFRS in different areas of national economies, and characterizes its current stage.

We believe that the collection of this conference contributions will be not only a source of ideas for further research, but also inspiration for solving practical problems which will motivate researchers further studies in this area.

The editors

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