Will the Czech accounting entities benefit from the Directive 2013/34/EU?

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Abstract

The European Union has published the Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings. According to the European Union, the reason and the sense of this Directive is to raise the competitive advantage and productivity of small and medium-sized enterprises. The EU Member States have to incorporate the rules of the Directive with their national law by 20 July 2015 at the latest during the year 2016. The intention of this paper is to determine and to evaluate the impacts of transposition of the Directive into the Czech Accounting Law.

Keywords: European Directives; accounting harmonisation; accounting systems; accounting principles; financial statements

1. Introduction

The regulation of accounting and reporting in the EU exists as early as the first directives about accounting were printed. Three directives complementing the Code of Accounting Practice and Financial Reporting were adopted and then they became of fundamental principles of the European Commission to harmonise the accounting rules. The point of reference was following:

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• Fourth Council Directive 78/660/EEC of 25 July 1978 especially focused on the content of the financial statements of big and medium-sized capital companies. This directive was thought as the most important rules in the accounting system in Europe.
• Eighth Council Directive 84/569/ECC of 10 April 1984 conditioning qualifying requirements for profession of auditor essential to verify competently the financial statements.

First two directives of Council of the European Community (the fourth and seventh) have been replaced by the only Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings (further Directive). The EU Member States have to incorporate the rules of the Directive with their national law by 20 July 2015 at the latest during the year 2016. According to the European Union, the reason and the sense of this Directive is to raise the competitive advantage and productivity of small and medium-sized enterprises. Considering small and medium-sized enterprises constitute the inherent part of sociality of the EU, the Directive could influence the economy and the economic growth of the European Union as a whole. The low participation of small and medium-sized enterprises in entrepreneurship in the single market (cross-border activities) in comparison with big-sized enterprises is caused by various matters. Nerudová, Bohušová (2006) consider as fundamental matter of fact obstacles which result from disunited accounting systems in the EU concerning small and medium-sized enterprises. The objective of the Directive and its rules is to harmonise requirements for very small, small and medium-sized enterprises in the EU and to reduce the administrative burden thus to improve their business environment. The articles of the Directive allow Member States to allow to very small and small accounting entities certain simplifications or even immunity from certain obligations which are typical for medium-sized and big-sized enterprises. At the same time, the Directive allows Member States to express the will upon application into national legislation however this application has to be in order to achieve the objective and the rules of the Directive. Starting point for specific provisions of the Directive is Generally Accepted Accounting Principles (GAAP). A significant element of the Directive is a principle “substance over form” when reports of items in financial statements have to be in accordance with economic and commercial gist of transaction. However, this principle is under command of each Member State so the enterprises can be exempt from this principle. Each Member State can also reduce application of Principle of Materiality only to a reporting and publishing (Directive 2013/34/EU). The possibilities of simplification or immunity is thus concerned especially indication, information and disclosure in the financial accounts, process for drawing up and publishing the financial statements, process for drawing up and publishing of annual reports, verification of financial accounts and annual reports by auditor (Účetní zpravodaj, 2014). However, Glogar (2015) emphasis that it is important to administrative burden of accounting entities would be adequate to benefits at the same time. Starting point for simplification or immunity from certain accounting duties is classification of accounting entities according to the size. The European Commission published The Recommendation 2003/361/EC where the partial distinction of enterprises was made in 2003. This Recommendation has been used for 10 years and it is very the Directive which made another distinction (classification) of enterprises by size (European Commission). Dubský (2015) says that the Directive regulated the values of criteria for very small and small enterprises but the values of criteria have not been changed for middle-sized and big-sized enterprises.

With the effect from 1st of January 2016, the Act No 563/1991 Coll. of Accounting and few others laws in the Czech Republic will be changed due to implementation of the Directive. For the first time, The Accounting Act implements classification of the accounting entities according to the size and also classification of consolidated groups. The fact, that the novel of the Accounting Act is significant is that there are approximately 400 000 enterprises of record and the majority will be very small and small-sized enterprises, less part of companies will be middle-sized enterprises and only very small part of companies will be big-sized enterprises (Důvodová zpráva MF ČR, 2015). At the same time and for the first time, the Czech Accounting Act defines the object of final account which is to provide the information for external users (Zákon o účetnictví, 2015). Also, there is an emphasis of meaning of audit of the financial statements. Much accounting duties with reference to the classification of enterprises are ordered to accounting entities liable to audit. It is logical because there is an emphasis on observance accounting principles in the respective accounting entities (Gláserová, 2015).
2. Materials and Methods

The main intention of this paper is to determine and to evaluate the impacts of transposition of the Directive into the Czech Accounting Law. This paper is focused on core areas which are: classification of the accounting entities according their sizes, classification of consolidated groups, obligation of accounting entities liable to audit and obligation of accounting entities in the field of drawing up and publishing of particular parts of financial statements.

Starting point of this paper is an analysis of the Directive then there is an identification of new matters of fact which can influence the laws in the Czech Republic. The paper from Germany has the biggest meaning of existing papers concerning this subject (Kaufhold, 2015). We can presume that the new papers from the rest of Member States will be created in 2016. The emphasis of this paper is a classification of accounting entities by size including fixation theirs accounting obligations. Then, a comparison of Accounting Act before and after 1 January 2016 is made as well as the differences. After that, there is an identification of the most stricken accounting entities with the Directive. Consequently, there is an upward revaluation of impacts of the Directive on Generally Accepted Accounting Principles, in particular the impacts on the principle of a true and fair view and on the precautionary principle. In the end, there is an assessment of the signification of compulsory audit of financial statements concerning the new classification of enterprises by size.

The assumption of this paper is a collection of information about the subject. The theoretical developments have been acquired from Czech a foreign literature relating the subject, but especially from the Accounting Act effective from 1st January 2016. The other information was founded on the internet. In this paper, the methods of description, comparison, analysis, logical thinking and deduction are used. The final results are illustrated in the tables. In the end, the method of synthesis is used.

3. Results and discussion

3.1. Categorization of entities

The main change in the amendment to the Czech Accounting Act is a categorization of enterprises according to three criteria (total assets, net sales, average number of employees) as you can see in Table 1.

Table 1. Categorization of entities according to Directive 2013/34/EU and amendment to the Czech Accounting Act.

<table>
<thead>
<tr>
<th>Category of enterprise</th>
<th>Total Assets</th>
<th>Net Sales</th>
<th>Average Number of Employees</th>
<th>Condition: to the Balance Sheet Day does not exceed no more than</th>
<th>Representation of enterprises in CZ (estimate in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU Directive (in thousands EUR)</td>
<td>Amendment to the Czech Accounting Act (in thousands CZK)</td>
<td>Amendment to the Czech Accounting Act (in thousands CZK)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Micro</td>
<td>350</td>
<td>9,000</td>
<td>750</td>
<td>18,000</td>
<td>10</td>
</tr>
<tr>
<td>Small†</td>
<td>4,000</td>
<td>100,000</td>
<td>8,000</td>
<td>200,000</td>
<td>50</td>
</tr>
<tr>
<td>Medium‡</td>
<td>20,000</td>
<td>500,000</td>
<td>40,000</td>
<td>1,000,000</td>
<td>250</td>
</tr>
<tr>
<td>Large</td>
<td>20,000</td>
<td>500,000</td>
<td>40,000</td>
<td>1,000,000</td>
<td>250</td>
</tr>
</tbody>
</table>

Source: Custom processing based on EU Directive and Explanatory Report of Czech Ministry of Finance

† Small is the one, which is not micro.
‡ Medium is the one, which is not micro nor small.
Table above implies that Czech Republic implemented into national law almost the same evaluation criteria as stated in the directive. In connection with setting the criteria levels arises question whether the same levels are suitable for use in Czech Republic. EU directive provides option for member states to change levels to higher values. However, micro and small enterprises must not exceed 6,000,000 EUR of Total Assets and 12,000,000 EUR of Net Sales. In this context some of the member states have set up different criteria in comparison to Czech Republic. Example can be Slovakia or Germany, where on 1st of January 2016 also enters into force an amendment to the Accounting Act. Categorization in Slovakia has only three categories, which are micro, small and large. Criterion for micro are bellow recommended level for Net Sales. The main difference can be seen in criterion for Average Number of Employees, where is value 50 for large enterprises ("Zákon o účtovníctve", 2002). In comparison to the EU directive we can consider this to be a significant difference. Opposite situation can be observed in German Accounting Act, where for small enterprises there are higher values for Net Sales and Total Assets in comparison to the EU directive (Kaufhold, 2015). Germany has values higher by one third, when compared to the Czech Republic.

Representation of enterprises is presented in the Basis for conclusions of Czech Ministry of Finance. It is assessed using the data from Czech Statistical Office. Here should be mentioned that Czech Statistical Office categorization is based only according to one criterion, which is an average number of employees. In case the enterprise employs 1–9 employees, it is classified as a micro enterprise, when enterprise employs 10–99 employees, it is classified as a small enterprise, enterprise with 100–249 employees is considered to be a medium enterprise and finally companies exceeding 250 employees are denoted as a large enterprises.

From total number of registered subjects in Czech Republic the majority will be micro and small enterprises, smaller part will be medium sized and only very small share will be large enterprises and so called subjects of public interest, as was mentioned before. Information mentioned above are also evident in Table 1, from which implies that more than 90% of enterprises are micro and small enterprises.

### 3.2. Categorization of consolidated groups

In accordance with the introduction of enterprises categorization there was also implemented classification of consolidated groups as small, medium and large.

<table>
<thead>
<tr>
<th>Category of consolidated group</th>
<th>Total Assets</th>
<th>Net Sales</th>
<th>Average Number of Employees</th>
<th>Condition: to the Balance Sheet Day does not exceeds no more than</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU Directive (in thousands EUR)</td>
<td>Amendment to the Czech Accounting Act (in thousands EUR)</td>
<td>EU Directive (in thousands EUR)</td>
<td>Amendment to the Czech Accounting Act (in thousands CZK)</td>
<td></td>
</tr>
<tr>
<td>Small</td>
<td>4,000</td>
<td>100,000</td>
<td>8,000</td>
<td>200,000</td>
</tr>
<tr>
<td>Medium</td>
<td>20,000</td>
<td>500,000</td>
<td>40,000</td>
<td>1,000,000</td>
</tr>
<tr>
<td>Large</td>
<td>20,000</td>
<td>500,000</td>
<td>40,000</td>
<td>1,000,000</td>
</tr>
</tbody>
</table>

Source: Custom processing based on EU directive and Explanatory Report of Czech Ministry of Finance

Here also applies that Czech Republic implemented in its national law almost the same values for criteria as those specified in EU directive. Small number of enterprises in Czech Republic does not have an obligation to assemble

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consolidated financial statements. The only exception are groups with at least one enterprise which is subject of public interest. Therefore, the amendment to the Czech Accounting Act tightens obligation to assemble consolidated financial statements (small consolidated groups in case when there is at least one subject of public interest). Based on this fact we can expect that number of consolidated groups which are obligated to prepare consolidated financial statements will increase.

3.3. Audit obligation for enterprises in area of Financial Statement and publication of their parts

The accepted principle in the amendment of Accounting Act to the Czech Republic is that an exemption from certain accounting requirements should be applied to those enterprises, which are not obligated to have the Financial Statement audited. Based on the analysis of the amendment to the Czech Accounting Act it is possible to further divide the categories in connection with an obligation to verify the accuracy of the Financial Statements by the auditor. Considering this we can divide the enterprises into following categories: micro enterprises without the obligation to audit, micro enterprises with the obligation to audit, small enterprises without obligation to audit, small enterprises with obligation to audit, medium enterprises and large enterprises. Medium and large enterprises are always obligated to audit.

Table 3. Obligation of entities with respect to their categorization.

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
</tr>
<tr>
<td>Micro A</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
</tr>
<tr>
<td>Small</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
</tr>
<tr>
<td>Small A</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
</tr>
<tr>
<td>Medium</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
</tr>
<tr>
<td>Large</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
</tr>
</tbody>
</table>

Source: Custom processing based on amendment to the Czech Accounting Act

The obligation to audit will apply only for a very small amount of micro and small enterprises. It will be obligatory for those enterprises which it provides a special law regulation.

As shown in Table 3 and also as Čížek (2015) mentioned – micro and small enterprises, which are not obligated to audit their Financial Statement, are not obligated to disclosure their Profit and Loss Statement. Therefore, they disclose only Balance Sheet and Appendix, so the explanatory power and options for financial analysis are limited. We can see reduction of administration duties mainly for these enterprises. However, exempting these enterprises from obligation listed above has negative impact on basic accounting principles – in particular, the principle of prudence and of course the principle of true and fair presentation of accounting. It can be assumed that these enterprises will report according to the prudence principle only those facts which will be tax expense for tax purposes in the same time. Above mentioned causes that these enterprises will not be careful enough to anticipate risk situations, which could cause lower profit in future periods. Simultaneously accounting will not be able to provide true and fair presentation of reality, which is basic requirement for accounting.

4. Conclusion

It can be stated that amendment Czech Account Act uses almost all options for simplifications or exemptions allowed by EU directive in order to reduce administrative burden of micro and small enterprises.
If we should evaluate respective values for criteria related to categorization of enterprises and consolidated groups, we could state that Czech Republic is consistent with the EU directive. The research has traced that in member states were the values of criteria set up on lower but also on higher values when compared with recommended levels of EU directive. The changes are in accordance with economic situations of respective states. Can be argued whether the levels of criteria in Czech Republic which are based on EU directive are suitable for Czech Republic economic situation and whether the levels shouldn’t be on lower values because according the categorization we can assume that more than 90% of enterprises will be classified as a micro or small enterprise. Nevertheless, these percentages must be taken only as an estimate, it is assessed using the data from Czech Statistical Office, where the enterprises are categorized only according to one criterion which is the number of employees. Another factor which could have negative impact to the accuracy of expected representation of enterprises is conflict between the number of total registered subjects and the number of subjects from which the numbers of subjects for each category were generated. The reason for this is non-disclosure of Financial Statements or respective criteria.

Finally, it must be emphasized that the amendment to the Czech Accounting Act was inevitable as it is a transposition of EU directive. The EU directive must be implemented by all member states into their national law. As was mentioned in this paper, it is certain that the practical application of this amendment to the Czech Accounting Act will affect basic accounting principles. Only time will show whether the main goal of EU directive, which was to reduce administrative burden of micro and small enterprises, will no be at the expense of the true and fair presentation of accounting.

References