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SELECTED PROBLEMS OF FINANCIAL REPORTING UNDER THE CZECH LEGISLATION AND INTERNATIONAL FINANCIAL REPORTING STANDARDS

Abstract: The aim of this paper is to compare the statutory conditions for the reporting of accounting information pursuant to Czech legislation and the international financial reporting standards (IFRS/IAS). The paper is divided into three parts. The first part deals with the comparison of basic preconditions for submission, compilation and publishing of financial statements pursuant to the principles of Czech legislation and the international financial reporting standards (IFRS/IAS). It is followed by a comparative analysis aimed at the statement of financial position. Finally the last part compares the requirements imposed on the contents and scope of the appendices to the financial statements. At the end of this paper the most significant differences of financial reporting according to Czech legislation and IFRS/IAS are presented. The aim of this paper is not to research and quantify impacts of different reporting of individual accounting items.

Keywords: financial reporting, statement of financial position, income statement, valuation, Czech legislation, International Financial Reporting Standards (IFRS).

1. Introduction

Globalization has led to an increase in local markets, wider competition, and lower barriers to international exchange, exposing smaller as well as larger companies to similar international problems. This situation influences financial accounting and reporting financial statements. Consistent with its intent to address the need for international comparability in terms of financial reporting, the International Accounting Standards Board issues and constantly updates a set of the International Financial Reporting Standards (hereinafter referred to as “IFRS/IAS”) for listed companies, and in July 2009 it also issued a simplified IFRS for small and medium-sized entities. Accounting regulations (and practices) in countries of continental Europe are not fully harmonized, there are conceptual problems in the current regulations and these regulations are influenced by taxation and are of a rule-based approach.

The paper deals with a comparison of the statutory conditions for the reporting of accounting information under Czech legislation and the international financial reporting standards (IFRS/IAS). The first part of the paper deals with a comparison of the basic preconditions for the submission, compilation and publication of the financial statements under the principles of Czech legislation and the international financial reporting standards (IFRS/IAS). The second part of the paper introduces a comparative analysis aimed at the balance sheet. The third part consists of a comparison of the requirements imposed on the contents and scope of the notes to the financial statements. At the end of this paper the most significant differences of financial reporting, according to Czech legislation and IFRS/IAS, are presented. The aim of this paper is not to research and quantify impacts of different reporting of individual accounting items.

2. Basic preconditions for the submission, compilation and publication of financial statements

2.1. Determination and scope of the package of financial statements to be submitted under Czech legislation

In accordance with Czech legislation, financial statements represent a part of the so-called **annual report**, a complex package of documentation, comprising of (pursuant to Section 18 of the Act No. 563/1991 Coll., Accounting Act) the **Statement of financial position (balance sheet)**, **Income (Profit and Loss) statement** and **notes** to financial statements containing general information on the accounting unit and explaining the information contained in the balance sheet and the profit and loss statement in more detail (i.e. information on accounting methods and principles applied, if the accounting methods or principles were changed, it must be noted in these notes). The Accounting Act further requires that the notes must contain information on outstanding liabilities from social security and contribution to the state employment policy, on the amount of outstanding liabilities from public health insurance and finally the amount of outstanding tax liabilities (imposed by the local tax authorities). The financial statements package may also include the **cash flow statement** and the **statement of changes in equity**.¹ The Accounting Act is further

¹ In accordance with the Accounting Act (Section 19, par. 9) the accounting units which are business companies issuing securities listed on a regulated market of securities in the European Union's Member States shall apply international accounting standards (International Financial Reporting Standards), as governed by the European Community's law, to keeping their accounting and preparing their financial statements. It seems to be evident that the Czech legislators did not acquaint themselves with IFRS/IAS standards thoroughly, as it is impossible to keep accounts according to them. The consolidating accounting units issuing securities listed on a regulated market of securities in the European Union's Member States must also follow IFRS/IAS standards while preparing their consolidated financial statements and annual reports. For other consolidating accounting units the application of IFRS/IAS standards is optional. All the other accounting units must prepare their financial statements in accordance with Czech legislation.

implemented by Decree No. 500/2002 Coll., defining the contents of individual statements in more detail, and the Czech Accounting Standards (for entrepreneurs CAS 001 – 023) outlining the Accounting Act and Decree No. 500/2002 Coll. in detail [25; 26].

The Czech legislation also determines the required scope of the financial statements. Companies' financial statements must be verified by the auditor who shall prepare the financial statements and the related appendices to the full extent (i.e. including the statement of changes in equity and cash flow statement). These relate especially to public limited corporations, investment companies and funds. Cooperatives and other trading companies have the same obligation only if two out of a total of three statutory limits are exceeded in two consecutive accounting periods.² Also these entities must have their financial statements verified by the auditor. Other accounting units may prepare their financial statements in a simplified scope [25].

2.2. Determination and scope of the package of financial statements to be submitted pursuant to IFRS/IAS standards

The issues associated with the financial statements, their presentation, drafting and publishing, are extensively covered in the Conceptual Framework for Financial Reporting, IAS 1 – Presentation of Financial Statements³ and IAS 7 – Cash Flow Statements. The **Conceptual Framework** [22] sets the goal, users, basic preconditions for the preparation of financial reporting, qualitative characteristics of financial statements, scope, methods for recognition and valuation of basic elements of final accounts and capital preservation. **IAS 1** [1; 5; 6; 12] deals with the purpose of financial reporting, defines the components of financial statements and the basic concepts for the fair presentation of financial position and performance of an entity, the principle of a going concern, accrual basis of accounting, consistency of presentation, materiality and aggregation, offsetting, comparative information. It further defines the structure and content of financial statements in general (statement of financial position as at the end of accounting period, i.e. balance sheet, statement on comprehensive income for the relevant accounting period, i.e. income statement, and the statement of changes in equity) and appendices (notes) to the financial

² According to the Accounting Act the following conditions shall apply: 1) the balance sheet total exceeds CZK 40 million; 2) net annual turnover exceeds CZK 80 million; 3) average adjusted headcount exceeds 50 employees.

³ IAS 1 went through many revisions and amendments. In 2004 its name was changed (from original IAS 1 – Preparation and Presentation of Final Statements) as well as its content. Another amendment came in April 2007 in particular with regard to requirements for presentation of financial statements and terminology used. In 2008 the new classification of derivatives (short-term and long-term) was introduced. The same was done in 2009 for convertible tools, with effect from 1.1.2010. IAS 1 is a kind of follow-up to the Conceptual Framework, extending and specifying the conceptual framework requirements in more detail.

statements. **IAS 7** [1; 5; 12; 15] deals with the presentation and reporting of the cash flows of an entity. The aim is to make the reporting and valuation of certain accounting items more accurate. It defines the individual accounting items and sets the criteria for their recognition (reporting) in financial statements as well as the general requirements for their publishing.

While preparing the financial statements, the standard **IAS 8** – Accounting Policies, Changes in Accounting Estimates and Errors must be followed to [18; 23; 24]. *Accounting policies* are the rules and procedures the company uses to prepare the financial statements (i.e. specific principles, bases, conventions, rules and procedures adopted by a company to prepare and report financial statements). In some cases the standard allows to chose from two policies (basic and alternative). The company should always chose the policy that will help to present the economic reality (financial position and performance) of the company more fairly. The selected accounting rule may only be changed when required by the applicable standard (IFRS) or when a more reliable presentation of the financial position, performance and cash flows can be achieved. The change shall be applied retrospectively (i.e. also to past financial statements). The accounting unit must present the nature, reasons and value impact of the change in the current as well as in past periods. In case the retrospective application is impossible or impractical, the new accounting policy must be applied on a prospective basis (i.e. in the current period and possibly also in subsequent periods) starting from the most recent period the change may be applied to. A *change in accounting estimate* is an adjustment of the carrying amount of an asset or a liability or the amount of the periodic consumption of an asset (e.g. for uncollectable claims, obsolete inventory, depreciation/amortization of assets with regard to the life time determined etc.); the changes in accounting estimates must be carried out to make the original estimations more accurate based on new findings – therefore they are not considered as corrections of errors. Changes in the accounting estimate shall be recognized within the future timeline. *Errors* are specified as prior period errors due to which the past financial statements cannot be considered as reliable (e.g. mathematical mistakes, incorrectly applied accounting policies, oversights, misinterpretations of facts, frauds, etc.). Material errors of past periods must be corrected retrospectively. In such cases the nature of the error, corrected values and – in case the error could not be corrected retrospectively – the reasons for the error correction infeasibility, must be stated [1; 5].

From the above mentioned standards it is obvious that as at the end of each accounting period, companies are obliged to present to the users their **balance sheet** showing the true information on their financial position, **profit and loss statement** that should truly show the financial performance of the company (comprehensive income for the relevant accounting period), **cash flow statement** truly showing all cash flows in the company. Financial statements according to IFRS/IAS standards further include **statement of changes in equity** showing either all changes to equity or only some of them (those that do not relate to transactions with equity holders).

The financial statements are supplemented by **notes to financial statements**. They contain the accounting policies used and explanatory comments to individual statements. The standards apply both to individual and consolidated financial statements [12; 13; 14].

It is clear that the components of the final statements pursuant to Czech legislation differ from the statements presented according to IFRS/IAS standards. IFRS/IAS standards require the presentation of the package comprising of four statements, whereas the Czech legislation requires only two statements (balance sheet and profit and loss statement). The requirement for the presentation of the statement of changes to equity results indirectly from the requirements for the scope of notes applicable to companies subject to statutory audit. The cash flow statement may be included if compiled by the company, however there is no strict requirement set by Czech legislation to present this statement by Czech companies with effect until the end of 2009. Unlike in IFRS/IAS standards, Czech legislation does not require the retrospective correction of data in case of changes in the accounting policy.

2.3. General preconditions for drafting financial statements

In accordance with *Czech legislation*, the accounting units shall be obliged to keep their accounting in a manner which will enable them to draw up the financial statements giving a true and fair representation of the object of accounting and the financial position of the accounting unit, i.e. a true and fair representation of assets, liabilities, equity, costs, revenue and the result of business. The representation is regarded as true if the contents of the items in the financial statements correspond to their actual position, and these items are shown in accordance with the relevant methods of valuation, depreciation, implementation of adjustments and provisions as well as other accounting procedures, methods and policies prescribed for such accounting unit on the basis of the Act on Accountancy and the implementing regulations or the Czech accounting standards. These accounting procedures must be used in a manner leading to a true depiction. Where an accounting unit may choose from two or more accounting procedures and the selected procedure would conceal the actual financial position, the accounting unit must choose the procedure which would fairly reflect the actual position. No arbitrary switching of methods is allowed [14; 25; 26].

Pursuant to *IFRS/IAS standards*, the general preconditions for the drafting and presentation of financial statements are covered in the Conceptual Framework. The leading principles are the accrual basis of accounting and the going concern principle.⁴

⁴ According to this concept, an entity preparing IFRS financial statements is presumed to be a going concern with no intention to quit or initiate bankruptcy/liquidation proceedings or to restrict the business significantly (currently IAS 1 quantifies this period as at least 12 months following the financial statements date). If management has significant concerns about the entity's ability to continue as a going concern, the uncertainties must be disclosed.

According to IAS 1, a **fair presentation** may only be achieved by the proper application of individual international standards and the presentation of additional/supporting information. The standard, however, allows for a departure from IFRS requirements in extremely rare circumstances when the management may conclude that compliance with IFRS requirements would be so misleading that it would conflict with the objective of the financial statements. Such a departure will be, however, clearly noted including the relevant standard and quantification/justification of the financial impact on net profit or loss, assets or liabilities, equity or cash flows of the company. Later on, the **consistency of presentation** is required, i.e. the presentation and classification of items in the financial statements shall be retained from one period to the next. Each **material class of similar items** must be presented separately. Immaterial items may be **aggregated** with items of a similar nature or function and do not need to be presented separately. In general **no offsetting** is allowed (except for cases when offsetting is required or allowed by the relevant standard or interpretation, e.g. in the case of deferred tax pursuant to IAS 12 or adjustments to inventories pursuant to IAS 2) [12; 15; 17].

The Conceptual Framework [1; 5] precisely defines the general accounting items as well as the criteria for their recognition and reporting. 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. Such economic benefits must be adequately probable, i.e. it must be feasible that future economic benefits will occur. Moreover the asset must be reliably valuable. A **liability** is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits. Such an outflow from the entity of resources embodying economic benefits must again be adequately probable. Liability must be reliably valuable. **Equity** is the residual interest in the assets of the entity after deducting all its liabilities. **Incomes** are increases in economic benefits during the accounting period in the form of inflows or the enhancement of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants. Income must be reliably measurable and adequately probable. Expenses are decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants. A basic principle for the reporting of expenses is their connection with the incomes achieved (matching principle). The accounting item is recognizable for reporting if the following **two preconditions** are met: the item must comply with one of the above mentioned definitions and must be reliably valuable.

Table 1 shows the comparison of qualitative characteristics of reporting as required by Czech legislation and IFRS/IAS standards.

Table 1. Qualitative characteristics pursuant to Czech legislation and IFRS/IAS standards

Czech legislation	IFRS/IAS standards
<i>Reliability</i>	
Financial statements must give a true and fair representation of the subject of accountancy and show the financial, property and income situation/position in realistic figures. Information presented in financial statements must be complete and timely from the statements users' point of view.	Information is considered as reliable if it is not biased and does not include material errors, gives a true and fair representation of the actual position, shows the essence and economic reality of the accounting unit disregarding legal ownership, does not contain overestimated revenues and assets or underestimated expenses and liabilities.
<i>Comparability</i>	
Information presented in financial statements must be reported, compiled and published in a manner allowing their comparison with the previous periods of the same accounting units as well as with other accounting units. The precondition is the consistency of methods applied, balance continuity and a thorough description/specification of all material changes and deviations between individual periods (in notes) incl. justification/reasons and description of impact/influence on balance sheet items and the result of business.	Users must be allowed to compare the items presented in financial statements as well as additional information with regard to time (historic data for the relevant company, at least for the current and the previous accounting period) and place (multiple companies). A basic precondition for comparability is the consistency of methods used (valuation, depreciation etc.). In case of any change in reporting, the accounting unit must reclassify the comparable data based on the newly implemented methods and procedures. The substance (principle), amount and reasons for each reclassification must be documented and reported. Should it be impossible to reclassify the comparable amounts, again the reasons must be stated (and the description of the consequences of potential reclassification).
<i>Understandability</i>	
The content of financial statements must be prepared, presented and published in a way so that the informed users, having a decent knowledge of the accounting methods applied, receive a correct impression of the property, income and financial position of the accounting unit.	The basic precondition is the sufficient education of users of the financial statements in accountancy and their ability to understand the reported data – complex information should not be omitted from the financial statements just because they may be incomprehensible for certain users.
<i>Relevance</i>	
Financial statements must contain all the relevant information and facts, whereas material data may be only excluded from the financial statements when incomprehensible for the users. The materiality is assessed especially with regard to information reported in notes to financial statements. Information is considered as material in cases of its omission or incorrect presentation may affect decisions by users of such information.	All information considered as material or significant must be included in the financial statements. Information is considered as material in cases when its omission or incorrect presentation may affect decisions by users of such information regarding the accounting unit. Quantification of such materiality is however not covered by international standards.

Source: author's own work in accordance with [26; 1].

From the information above it is clear that the definition of a true and fair representation in Czech legislation and IFRS/IAS standards is considerably different. In accordance with Czech legislation, a true and fair representation is achieved by following the applicable legislation and related regulations, whereas IFRS/IAS standards admit a certain deviation from the standards in cases when compliance is so misleading that it would conflict with the objective of the financial statements – the true representation of reality always prevails. From this perspective the reliability of financial statements may also be perceived differently. The requirements for the comparability of financial statements pursuant to IFRS/IAS standards are stricter – in cases of any change the reclassification shall be applied even to financial statements from past periods. On the other hand, Czech legislation only requires the publication of the potential impacts/consequences in the notes to the financial statements for the current period. The requirements also differ in cases of comprehensibility and relevancy – unlike Czech legislation which allows for the exclusion of certain information just because they may be incomprehensible for some users, IFRS/IAS standards assume an adequate knowledge/education of users and do not allow to exclude any information from the financial statements. And again – unlike IFRS/IAS standards – Czech legislation does not define the basic accounting items and criteria for their recognition, which may lead to the incorrect reporting and valuation of balance-sheet items.

2.4. Valuation of assets and liabilities

Czech legislation (Accounting Act) admits the following valuation bases [26]:

1. As at the moment of accounting transaction realization, the following methods of valuation are possible: acquisition costs, production costs, nominal value, replacement acquisition costs. In cases of a decrease of inventory or securities, the valuation is made on the basis of weighted arithmetical average, or using the “FIFO” method (the first price used for valuation of increase in assets is used as the first price for valuation of decrease in assets).⁵ In general, these are the values determined on a **historical basis**. Assets obtained free of charge shall be valued by **current cost** (in Czech legislation referred to as the replacement acquisition cost) [7; 9].

2. At the moment of financial statements preparation, the Accounting Act allows for the revaluation of selected items to their **real (fair) value**. For this purpose the real value shall either mean market value, valuation by a qualified estimation or expert opinion or the value determined pursuant to other regulations (e.g. in accordance with the Act on investment companies and investment funds) [8; 10; 11; 16].

⁵ Since 1.1.2009, cultural relics, museum collections, items of cultural value and religious structures, unless their acquisition price is known, are valued at CZK 1.00 (this especially applies to state-owned assets).

The Conceptual Framework for IFRS/IAS standards determines and characterizes these valuation bases: **historical costs, current costs, net realizable value and net present value (discounted)** [1; 2; 5].

Considering the above mentioned facts, it is obvious that the Czech system does not evaluate assets and liabilities by net present value.

3. Balance sheet compiled pursuant to Czech legislation and IFRS/IAS standards

In Czech legislation the structure and designation of individual balance sheet items for entrepreneurs shall be governed by Decree No. 500/2002 Coll. The items are stated separately in the given order. A more detailed breakdown of these items may be applied if the required order remains unaffected. The balance sheet items may be consolidated if:

- the amount is immaterial considering the obligation of a true and fair representation of the subject of accounting and the financial position of the accounting unit,
- such consolidation contributes to the better comprehensibility of information, provided that the consolidated items will be specified in details in the notes [14; 21; 26].

In the balance sheet for the current period the following is stated: the gross amount of assets (by individual items), i.e. without consideration of the adjustment entries and depreciation reserves, the amount of related adjustment entries and depreciation reserves (correction) and the net amount of assets, i.e. reduced by adjustment entries and depreciation reserves. Items of the balance sheet and the profit and loss statement showing a zero value in the previous and also the current period may be omitted. Each item in the balance sheet, in the profit and loss statement as well as in the statement of changes to equity shows, besides the current year value, also the value for the immediately preceding accounting period (i.e. the previous year). If the information presented for the previous and for the current period is not comparable, the information for the previous period must be adjusted, considering the principle of relevancy pursuant to Section 19, par. 6 of the Act on Accountancy. Each adjustment of information for the previous accounting period or keeping the incomparable information must be justified in the notes [14; 25; 26].

Financial statements are prepared in Czech currency and the individual items are stated in whole thousands of Czech crowns.⁶ The items “total assets” and “total liabilities” must be equal. The operating result for the relevant accounting period, as shown in the profit and loss statement, must be equal to “Profit/loss – current year” in the balance sheet.

Table 2 shows the content and structure of a simplified balance sheet, as required by Czech legislation. This structure is only allowed if the financial statements of the

⁶ Since 2008 accounting units with assets (net) of at least CZK 10 billion may state the individual items in whole millions of Czech crowns. This must be reflected in all parts of the financial statements.

Table 2. Structure and content of the balance sheet (simplified version) pursuant to Decree No. 500/2002 Coll.

Assets	Liabilities
A. Receivables from subscriptions	A. Equity
B. Fixed assets	A. I. Registered capital
B. I. Tangible fixed assets	A. II. Capital funds
B. II. Intangible fixed assets	A. III. Reserve funds, statutory reserve account for cooperatives and other retained earnings
B. III. Long-term financial assets	A. IV. Profit/loss – previous year
C. Current assets	A. V. Profit/loss – current year
C. I. Inventory	B. Other sources
C. II. Long-term receivables	B. I. Reserves
C. III. Short-term receivables	B. II. Long-term payables
C. IV. Financial assets	B. III. Short-term payables
D. Accruals	B. IV. Bank loans and financial accommodations
	C. Accruals

Source: author's own work in accordance with [25].

accounting unit are subject to statutory audit (pursuant to the Czech Act on Accountancy). The audited companies must prepare the balance sheet in its full extent.

According to IFRS/IAS, assets and liabilities must be presented separately in the balance sheet (short-term and long-term). The division by liquidity is only possible if it gives more reliable and relevant information (from the most liquid to the least liquid). Assets are considered as short-term if the company expects their realization within the standard operating cycle of the company, and if they are – within 12 months following the balance sheet day – held in the company primarily for trading reasons, or if they are cash and cash equivalents with unlimited use. Short-term liability is defined as a liability the settlement of which is expected within the standard operating cycle of the company or within 12 months following the balance sheet day.⁷ Other items are considered as long-term. Table 3 shows the minimum requirements for the publication of balance sheet items pursuant to IAS 1. The items are mandatory, however accounting units may add other items relevant for the informedness of the users of financial statements [1; 5; 19; 23].

Other standards also apply to the published structure of balance sheet items. According to them it is necessary to present, either directly in the balance sheet or in the notes, a more detailed specification of long-term tangible assets, inventory, receivables and payables (divided for instance into receivables of companies within the group and other trade receivables, related entities, advance payments etc.), reserves divided into employee benefits and other reserves, equity by its individual

⁷ Short-term liabilities are even those payable after 12 months, provided they are business liabilities (from trading), debts towards employees etc.

Table 3. Basic structure of balance sheet – items required pursuant to IAS 1

Assets	Liabilities
<ul style="list-style-type: none"> • Property, plant and equipment • Investment property • Intangible assets • Financial assets (excluding investments accounted for using the equity method, trade and other receivables and cash and cash equivalents) • Investments accounting for using the equity method • Biological assets • Inventories • Trade and other receivables • Cash and cash equivalents • Assets held for sale 	<ul style="list-style-type: none"> • Issued capital and reserves attributable to owners of the parent • Non-controlling interests, presented within equity • Liabilities and assets for current tax • Deferred tax liabilities and tax assets • Provisions • Trade and other payables • Financial liabilities (excluding trade and other payables and provisions) • Liabilities included in disposal groups

Source: author's own work in accordance with [1 – IAS 1].

components etc. Special requirements are imposed on the publishing of information on stock capital.

We may conclude that the level of regulation with regard to the balance sheet (and other financial statements) is weaker under the IFRS/IAS standards than under Czech legislation. The conclusion is that the statements prepared pursuant to IFRS/IAS standards reflect the actual conditions and position of the relevant accounting unit that better complies with the principle of a true and fair representation. The uniform Czech reporting system would – on the other hand – provide a better comparability of individual companies. However the non-existence of any conceptual framework and the missing detailed specification of basic accounting items make this benefit much weaker.

4. Notes to financial statements pursuant to Czech legislation and IFRS/IAS standards

4.1. Definition of notes to financial statements pursuant to Czech legislation

The purpose of the notes is to comment, specify in more detail and amend the items of the balance sheet and the profit and loss statement. The basic form, content and requirements for notes to the financial statements are covered in the implementing decree issued by the Ministry of Finance.⁸ Pursuant to the Accounting Act the financial statements must contain [26]:

- first name and surname, the commercial name or other designation of the accounting unit, the seat or the home address or place of business if the latter differs from the former,

⁸ For entrepreneurs see Section 39 of the Decree No. 500/2002 Coll.

- the accounting unit's identification number, if allocated,
- legal form,
- subject of business or other activity, or the purpose for which the accounting entity was established,
- the balance-sheet day or some other day at which the financial statements are drawn up,
- the day when the financial statements were drawn up,
- signature record of the accounting unit's statutory body.

The regulation applicable to the preparation and content of the notes to the financial statements does not set a mandatory **form of notes**, but suggests the company prepared the notes in a descriptive manner, in a table format or using a combination of both approaches.

The content of notes to financial statements submitted by audited companies that must publish their financial statements comprises of the following basic sections [25]:

- 1) general information,
- 2) information on accounting methods, general accounting principles and valuation methods applied,
- 3) additional information to the balance sheet and the profit and loss statement,
- 4) cash flow statement, if compiled,
- 5) statement of changes to equity.

Ad 1) General information. The general information shall include:

- Information pursuant to the legislation on accountancy,⁹ such as a description of the accounting unit, especially name, registered office, legal form, prevailing subject of business, date of formation or commencement of business activities, persons (physical and legal) with a controlling or significant influence on the accounting unit (including a statement of their percentage share), description of the changes and amendments in the corporate register in the relevant accounting period, description of the organizational structure of the accounting unit and the material changes during the relevant accounting period. Also it is required to state the names and surnames of the members of the statutory and supervisory bodies as at the balance sheet day.
- Names of trading companies and registered office of accounting units in which the company has a controlling or significant influence (including a specification of share in their registered capital).¹⁰

⁹ Especially pursuant to Section 18, par. 2 of the Accounting Act and Section 39, par. 1 of the Decree No. 500/2002 for entrepreneurs.

¹⁰ Moreover the possible agreements between partners should be stated here, establishing the decision-making rights, disregarding the amount of shares in such companies. The accounting unit must state the amount of equity and the economic result of such companies for the last accounting period, provided such information may be retrieved. Also the contracts on controlling influence or transfer of profit must be noted, if concluded.

- Average headcount (number of employees) during the relevant accounting periods and the number of controlling bodies.¹¹
- The amount of loans, credits (including interest rates and main conditions), provided securities and other fulfillments, such as the free provision of vehicles or other tangible and intangible assets, payments of pension supplementary insurance etc. Such fulfillments may be either monetary or non-monetary, provided to persons representing the statutory bodies or acting as members of management bodies of the company (including former members).

Ad 2) Information on accounting methods, general accounting principles and valuation methods applied. This section covers:

- All information on the application of general accounting principles, on accounting methods used and also the methods of valuation and depreciation.¹²
- Information on departures from accounting methods,¹³ their impact on assets and liabilities and the operating result of the accounting unit.
- On the basis of the relevant principles, the following is stated:
 - a) the method of determination of the depreciation allowances and adjustment entries, together with the source of information for the determination of their amounts,
 - b) the method of conversion of data in foreign currencies to Czech currency and the method for the determination of the real value of the relevant assets and liabilities,
 - c) a description of the model used by the accounting unit for the valuation of securities and derivatives using a real value, changes of such real value and changes in valuation by individual types of financial assets and methods of their recognition (posting in accounting books).¹⁴

Ad 3) Additional information to the balance sheet and the profit and loss statement. In this section the accounting unit states and then explains every single material item or group of items from the balance sheet or the profit and loss statement, as relevant for the analysis and evaluation of the financial and property state of the

¹¹ On top of that, the amount of personal expenses per employee and controlling bodies must be stated. The accounting unit shall further state rewards paid to persons acting as the statutory body and other members of statutory and supervisory bodies as well as potential financial liabilities with regard to former members of such bodies.

¹² Such information shall be stated the knowledge of which is relevant for the due assessment of the financial and property position of the company and its operating result, for the analysis of information contained in the balance sheet and in the profit and loss statement.

¹³ These are the methods pursuant to Section 7, par. 5 of the Accounting Act.

¹⁴ The legislation requires that the accounting unit states for each type of derived information on the scope and essence, including the main conditions and circumstances, that could affect the amount, time path and certainty of future cash flows as well as the table showing all changes of real value during the accounting period for the item "Valuation differences from the overvaluation of assets and liabilities".

company and its operating result. Moreover it shall – for material items of assets – state all increases/decreases.¹⁵ The notes must include:

- a) relevant information on assets and liabilities, especially an explanation of the amount reported in the item line “Establishment expenses”,
- b) overdue receivables and payables,
- c) receivables and payables with a maturity of more than 5 years as at the balance sheet day,
- d) lease of assets,
- e) rights of lien or easements imposed on the assets as well as the statement of transferred or provided security,
- f) material petty tangible and intangible assets not covered in the balance sheet,
- g) foreign assets covered in the balance sheet (e.g. assets in a rented company or any part thereof),
- h) total amount of liabilities not included in the balance sheet,
- i) pension liabilities and liabilities towards accounting units within consolidated groups shall be stated separately.¹⁶

In accordance with Section 19, par. 5 of the Act on Accountancy, the accounting unit must state each material event that happened in the period between the balance sheet day and the day of compilation of the financial statements.

Ad 4) Cash flow statement shall follow the requirements pursuant to Act No. 563/1991 Coll., on Accountancy, Decree No. 500/2002 Coll. and the Czech Accounting Standard No. 023.

Ad 5) Statement of changes to equity is – pursuant to Decree No. 500/2002 Coll. – recommended to be prepared and included in the financial statements of the company as a separate statement. The comments to this statement, especially regarding to individual reasons for equity increase/decrease shall be covered in the notes to the financial statements.

4.2. Notes to financial statements pursuant to IFRS/IAS standards

The requirements for the content of the notes to financial statements are stated in the IAS 1 standard. The purpose of the notes (comments) to financial statements is to present information about the basis of preparation of the financial statements and the specific accounting policies used to disclose any information required by individual

¹⁵ The notes should also state such material items that were not included in the financial statements or compensated by other items (e.g. retrospectively imposed income tax from incomes of prior periods, overview of reserves and long-term bank credits incl. interest rates and securities, deferred tax liability or receivable specification, etc.).

¹⁶ The additional information should further include the number and nominal value or valuation of stocks (shares) issued during the accounting period and information on exchangeable bonds, significant increases/decreases of individual components of equity. The accounting unit shall also prepare an overview of revenue from the sale of goods, products and services by individual activities and possibly also geographical locations of markets (if different).

IFRS standards that is not presented elsewhere in the financial statements, and to provide additional information that is not presented elsewhere in the financial statements but is relevant to the understanding of any of them. The notes should be cross-referenced from the face of the financial statements to the relevant note [1; 6; 12; 17; 23].

The notes shall further include general information on the company, particularly the name and the domicile, a description of key operations and principal activities, if it is part of a group, the name of its parent and the ultimate parent of the group, amount of dividends authorized for issue but not recognized as a distribution to owners during the period and the amount of any cumulative preference dividends not recognized.

The notes should normally be presented in the following order:

- 1) a statement of compliance with IFRS/IAS standards;
- 2) a summary of significant accounting policies applied (including the measurement/valuation bases used in preparing the financial statements),
- 3) supporting information for items presented in each financial statement in the order in which each statement and each line item is presented,
- 4) other disclosures including contingent liabilities and unrecognized contractual commitments and non-financial disclosures.

5. Conclusion

On considering the above mentioned facts, it becomes obvious that the most significant differences in the financial reporting pursuant to Czech legislation and the International Financial Reporting/Accounting Standards (IFRS/IAS) are:

1. The scope of the package of statements presented. While IFRS/IAS require a package consisting of four statements, Czech legislation requires only two (balance sheet and profit/loss statement). In this regard the Act on Accountancy states that “... *financial statements may also include the cash flow statement or the statement of changes to equity...*”^{17,18} The requirement for the presentation of the statement of changes to equity indirectly results from the requirements for the scope of financial statements to be submitted by companies subject to statutory audit. The cash flow statement may be included if compiled by the company, however there is no strict requirement set by Czech legislation to present this statement.

2. Level of regulation. IFRS/IAS give more freedom to companies with regard to the preparation of their financial statements. This has two consequences: the first

¹⁷ Act No. 563/1991 Coll., Accounting Act, Section 18, par. 1.

¹⁸ Through Act No. 304/2008 Coll., with effect from 1.1.2010, this provision was amended by the following text: “Selected accounting units shall prepare cash flow statement and statement of changes to equity always.” For this purpose the selected accounting units especially mean territorial self-governing units, allowance organizations, state funds and state organizational units.

one is positive – financial statements prepared and presented pursuant to IFRS/IAS standards reflect the actual conditions of the company which means they better meet the requirement for a true and fair representation of the company position and give more reliable information to their users; on the other hand a certain uniformity of Czech statements allows for better company-to-company comparability – the question however is whether such uniformity only applies to the designation of individual items (their terms) or is also reflected in the content of the items, i.e. to what extent the predicative capability of these statements is affected. We can conclude that the rather strong state regulation (through legislative standards) in the Czech Republic makes the application of IFRS/IAS standards more difficult for local companies. They can only prepare their statements pursuant to IFRS/IAS standards if they are listed on regulated markets with securities or if they are consolidated groups of companies. All the other business entities must report their financial statements in accordance with Czech legislation.

3. Scope of standards/regulations. Unlike IFRS/IAS standards that apply and were originally created exclusively for companies issuing securities registered on a regulated market of securities (usually big companies), Czech legislation is aimed at all entities being accounting units pursuant to the Act on Accountancy (i.e. small and medium-sized companies too).

4. The principle of true and fair presentation. Czech legislation defines true and fair representation as compliance with the applicable provisions of the Act on Accountancy and the related regulations. This however strongly contradicts the understanding of true and fair representation pursuant to IFRS/IAS standards, saying that the accounting unit should always reflect reality on the basis of its real economic essence.

5. Definition of general accounting items and criteria for their recognition. Unlike IFRS/IAS standards, Czech legislation does not include definitions of basic accounting items such as assets, liabilities, equity, expenses and incomes. This may result in the incorrect reporting and valuation of balance sheet items, making the correct comparability of companies within time and space difficult or even impossible.

6. Present value. The Czech accounting system does not include provisions on valuation at present value. IFRS/IAS standards require using the present value for the valuation of assets, the present value of which is lower than the actual value (the application of the principle of due caution in preparing financial statements).

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WYBRANE ZAGADNIENIA SPRAWOZDAWCZOŚCI KSIĘGOWEJ W ŚWIECIE CZESKICH PRZEPISÓW PRAWA I MIĘDZYNARODOWYCH STANDARDÓW SPRAWOZDAWCZOŚCI FINANSOWEJ

Streszczenie: Celem niniejszego artykułu jest porównanie uwarunkowań prawnych w zakresie prezentowania informacji księgowych według czeskiego ustawodawstwa oraz według Międzynarodowych Standardów Sprawozdawczości Finansowej. Artykuł podzielono na trzy części. W pierwszej części porównano podstawowe założenia w zakresie składania, opracowywania i publikowania sprawozdań finansowych w oparciu o czeskie przepisy o rachunkowości oraz Międzynarodowe Standardy Rachunkowości IFRS/IAS. Następnie dokonano analizy porównawczej bilansu. W ostatniej części porównano wymagania dotyczące treści i zakresu załącznika do sprawozdań finansowych. W zakończeniu artykułu przedstawiono najważniejsze różnice w sprawozdawczości finansowej w świetle czeskich przepisów prawa i Międzynarodowych Standardów Rachunkowości IFRS/IAS. Celem artykułu nie jest badanie i kwantyfikacja skutków odmiennego ujmowania poszczególnych pozycji księgowych.

Słowa kluczowe: sprawozdawczość finansowa, bilans, rachunek zysków i strat, wycena, czeskie przepisy o rachunkowości, Międzynarodowe Standardy Sprawozdawczości Finansowej.