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Introduction

These proceedings are published to accompany the 2nd year of the International Scientific Conference under the title IFRS: Global Rules & Local Use, taking place on October 10, 2014 at the Anglo-American University in Prague.

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Thematic distribution of papers and abstracts into sections:

- Plenary session – Academics and presentation of contributions
- Parallel section I – Financial Reporting and Implementation of IFRS. Theoretical Issues
- Parallel section I continue – Financial Reporting and Implementation of IFRS. Educational and Psychological Matters
- Parallel section I continue – Financial Reporting and Implementation of IFRS. Risk and Valuation Issues
- Parallel section II – IFRS Adoption, Cultural Differences and Ethical Issues. Value Relevance
- Parallel section II continue – IFRS Adoption, Cultural Differences and Ethical Issues. Non-Financial Disclosure
- Parallel section II continue – IFRS Adoption, Cultural Differences and Ethical Issues. Fair Value Issues and Factors Influencing Financial Markets

AUTHORS OF THE CD:

- doc. Ing. Irena Jindřichovská, CSc.
- Ing. Dana Kubíčková, CSc.

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INFORMATIVE ROLE OF CONSOLIDATED FINANCIAL STATEMENTS DRAWN UP IN ACCORDANCE WITH IFRS: THE CASE OF COMPANIES AT BANKRUPTCY-RESTRUCTURING PROCEEDINGS IN POLAND

Kinga BAUER
Cracow University of Economics
kinga.bauer@uek.krakow.pl

Joanna TOBOREK-MAZUR
Cracow University of Economics
toborekj@uek.krakow.pl

Abstract: In accordance with IFRS the objective of financial reporting is to provide useful information to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity (IFRS, The Conceptual Framework for Financial Reporting, §OB2). This objective is even more important in case of stock-market listed companies, because of their specificity. In the market economy, also among listed companies, are not only strong, successful entities but also weak, affected by severe crises, or even entities conducting bankruptcy-restructuring processes. The companies conducting bankruptcy with a possibility to make an arrangement, are entities continuing their business operations. At the same time, they have serious financial problems and a substantial doubt about an entity’s ability to continue as a going concern is probable. In order to reduce information asymmetry between stakeholders, the risk of bankruptcy and financial aspects of undertaken restructuring activities should be shown in the financial statements. The paper objective is to analyze principles and practices of presenting information about conducted bankruptcy with possibility to make an arrangement in consolidated financial statements made in accordance with IFRS. The problem of credibility of the information presented in consolidated financial statements in Poland in case of insolvency has been analyzed on the base of financial statements of two Polish stock-market listed companies, which conducted bankruptcy with a possibility to make an arrangement in recent years. In order to pursue the objective of this paper, literature studies and in-depth case study method has been applied.

Keywords: bankruptcy with a possibility to make an arrangement, consolidated financial statement, IFRS, Poland, restructuring

1. INTRODUCTION

The goal of a consolidated financial statement for a group of companies is to present reliable information about the financial condition of an entire group and condition of its assets. As a rule, a consolidated financial statement is a reflection of everything that has occurred in a given group within a year and prevents distortion of the true picture of the economic condition of the dominant entity.

On the other hand, the empirical research and scientific literature are full of critical remarks regarding accounting as the system which reflects an enterprise’s financial standing.

As shown by theoretical disputes, which pertain to various solutions, drawing up consolidated financial statements is no easy manner. The reports sometimes contain errors which
may deform the true economic condition of a group of companies. In practice, discrepancies occur about the current condition of an entity which is part of the group. This means that, the theory of accounting, its basic assumptions about true and fair view of an economic entity’s financial condition, is not inseparable from the praxis of drawing up and presenting consolidated financial statements.

At the same time, using the theory of accounting in practice may have a significant effect on how accounting solutions are perceived by society (Micherda, Świetla, 2014, p. 47). Utilizing the theory of accounting, which pertains to the usefulness of consolidated financial statements, should also positively influence society’s perception of information presented by companies listed on the stock market while the companies are in the process of bankruptcy with a possibility to make an arrangement. Stock-market listed companies which are in the process of declaring bankruptcy in the dominant or dependent company should strive to reduce information asymmetry between users of financial statements by publishing information about restructuring in a clear and reader-friendly manner.

The paper objective is to analyze principles and practices of presenting information about conducted bankruptcy with a possibility to make an arrangement in consolidated financial statements made in accordance with IFRS. The problem of credibility of the information presented in consolidated financial statements in Poland in case of insolvency has been analyzed on the base of financial statements of some Polish stock-market listed companies, which conducted bankruptcy with a possibility to make an arrangement in recent years.

In order to pursue the objective of this paper, literature studies and in-depth case study method has been applied.

2. THE ESSENCE AND LEGAL BASIS OF DRAWING UP CONSOLIDATED FINANCIAL STATEMENTS BY COMPANIES LISTED ON THE POLISH STOCK MARKET

Globalization and development of capital markets, including the stock exchange, are significant factors which influence the theory and practice of accounting, as well as the desire to unify financial statements on a global scale. In order for the financial markets to run smoothly, information of appropriate quality is required and also the guarantee that financial conditions of individual entities are comparable is needed, whilst trying to minimize economic risk. Furthermore, according to Ball (2006, p. 5) reductions in communication and information processing costs makes increased integration of financial reporting standards and practice almost inevitable.

Legal regulations, including the degree of investor protection, influence the capital market development, ownership scheme fragmentation and transparency requirements of an entity (Porta et al., 1999, p. 471–517). The term transparency has not been precisely defined in the context of financial reporting. However, as Barth and Schipper (2008, p. 173) defined “financial reporting transparency as the extent to which financial reports reveal an entity's underlying economics in a way that is readily understandable by those using the financial reports". They stated that: “theoretical research suggests that increased reporting transparency can reduce the cost of capital provided that transparency reduces information risk, and empirical research using a variety of measures of financial reporting transparency provides evidence of an association between transparency and cost of capital. Thus, research supports the notion that transparency is a desirable characteristic of financial reports”.

Transparency of stock-market listed companies is an important aspect not only for an enterprise but also for an entire country. Enterprises which wish to attract investors must do so by being a trust-worthy partner and disclosing detailed information about the condition of the enterprise (Aluchna, 2005, p. 11–17).

According to the theory of accounting, primary features of financial statements are their usefulness and intelligibility for the users. Whether they are useful or not depends on the content of a statement, content which is regulated by law through applicable accounting standards. The content
of a financial statement is, to some degree, influenced by securities trading law which regulates the range of additional disclosures for investors (Michalak, 2010, p. 69). The development of capital markets rises investors’ need for information, at the same time increasing information responsibilities of issuers. On the other hand, drawing up more and more complicated statements leads to increased costs and greater risk of the information being overtaken by competition (Świderska et al., 2010, p. 143). Consequently, this can result in limiting the information provided in a financial statement only to that required by law.

A group of companies does not constitute an economic entity and so has no legal personality. In the scope of the balance sheet law a group of companies is an accounting entity (Remlein, 2013, p. 20). In accordance with IFRS 10 a group it is a parent and its subsidiaries. Consolidated financial statements are “the financial statements of a group in which the assets, liabilities, equity, income, expenses and cash flows of the parent and its subsidiaries are presented as those of a single economic entity” (IFRS 10, Appendix A). The primary legal act which regulates the consolidation of financial statements in Poland is The Accounting Act, according to which (The Accounting Act, 2010, p. 55): “a parent undertaking which has its head office or place of management in Poland should prepare the annual consolidated financial statements of its group of companies or partnerships, covering the data of the parent undertaking and subsidiary undertakings of all levels, irrespective of their head offices, presented in such manner as if the group constituted a single undertaking; the financial statements should also cover the data of other subordinated undertakings”. At the same time, (The Accounting Act, 2010, p. 57): “consolidated financial statements of the issuers of securities (…) should be prepared in accordance with IAS”. It means that as a result of Poland’s membership in the European Union and the adoption of Regulation 1606/2002 of the European Parliament and the Council on the obligation to apply IAS/IFRS, consolidated financial statements of listed companies in Poland are prepared in accordance to international standards.

As Grabinski et al. stated (2014, p. 282): “the introduction of IFRS in Poland posed a major challenge for companies. (…) However, this process is beneficial for businesses”. IAS/IFRS should require high-quality, transparent and comparable information in financial statements and other financial reporting. The purpose of this approach is to help the users of financial information to make economic decisions (IFRS Foundation Constitution, 2010, §2).

3. USERS OF INFORMATION FROM CONSOLIDATED FINANCIAL STATEMENTS AND THEIR DEMANDS

Cyert and Ijiri (1974, p. 29) stated, that: “financial statements are not just statements reporting on the financial activities and financial status of a corporation. There are a product of mutual interactions of three parties: corporations, users of financial statements, and the accounting professions”. In accordance to IFRS “the objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity” (IFRS, The Conceptual Framework for Financial Reporting, §OB2).

The range of mandatory information to be provided in a consolidated financial statement depends on the receiver of the information included in financial statements of individual entities which are part of a group of companies and what is the purpose in providing this information to particular users. (Toborek-Mazur, 2010, p. 228). The users of consolidated financial statements should be treated with high priority in respect to determining the scope of information to be disclosed. Classification of the users of information can be made based on various criteria. The basic division is to set the type of required information. For this purpose, the users are divided into internal and external users. The internal users are owners of individual entities which are part of a group of companies, executive boards of companies, management of holding companies and analytical units which are part of the group. The range of information for this group must be broader
and more detailed than for external users. This is because property processed information is crucial in order to accurately evaluate current operations and make future decisions. The second group is composed of users which are not directly connected with the group of companies. This group includes the department of revenue, statistical offices, auditors, current and perspective lenders and investors (Toborek-Mazur, 2010, p. 261–262).

One of the most important groups of users of financial statements are without a doubt the capital providers. When making capital investment decisions, they are mainly interested in information which enables them to evaluate an entity’s ability to generate a positive financial flow and the ability of the company’s Board to protect and extend their investment (Zuchewicz, 2012, p. 81).

Research carried out in Poland by Dziwago (2011, p. 91–93) shows that, when individual investors now make a decision to buy stock, accounting and financial statement information is not a deciding factor but only aids the process. At the same time, based on observation of stock-market companies, it is clear that investors expect more transparency and full access to clear and reader-friendly financial data, put more pressure on the quality of information and being held accountable for it. In reference to companies listed on the stock market, market analysts in particular, expected a wider range of data than that on a financial statement and a more detailed financial data.

Research proves that, the range of financial reporting information varies depending on the user of the report. However, Luty believes that (2010, p. 128–129) amidst of other information, information about the continuation of business operations is significant for internal users (board, unions) as well as external, cooperating users (banks, contractors) and also non-cooperating users (owners of capital instruments). In the case of external users, the information about the continuation of business operations is a top priority on the information hierarchy. Another key information is the risk involved with the economic activities.

In connection with the above, information about bankruptcy proceedings being currently held for the purpose of making an arrangement in an entity which is part of a group of companies, will be of a high priority to the users of this information.

4. BANKRUPTCY WITH POSSIBILITY TO MAKE AN ARRANGEMENT AND THE INFORMATION IN CONSOLIDATED FINANCIAL STATEMENT

4.1 Essence of bankruptcy with possibility to make an arrangement in Poland

Bankruptcy with a possibility to make an arrangement in practice in Poland means that, an enterprise can continue business operations, however, a substantial doubt about an entity’s ability to continue as a going concern is highly probable. Legal basis of filing for bankruptcy are the same as during liquidation of assets procedures of an insolvent debtor, that is: bankruptcy shall be declared with respect to a debtor who has become insolvent. In accordance with The Polish Bankruptcy and Reorganization Law (art. 10, 11) it means, that:

- a debtor fails to perform his due financial obligations,
- a debtor also be deemed insolvent when the sum of his obligations exceeds the value of his assets, even if the debtor duly performs these obligations.

The court declares bankruptcy with the possibility to make an arrangement if it is determined likely that under the arrangement the creditors shall be satisfied to a higher degree than they would be satisfied as a result of conducting the bankruptcy by the liquidation of the debtor's assets.

Most bankruptcy proceedings in Poland are proceedings which lead to the liquidation of assets of an insolvent debtor. (Tab. 1). Still, annually over ten percent of bankruptcy proceedings held are proceedings which lead to an arrangement. Furthermore, work is currently underway in Poland to change the bankruptcy law so that it facilitates a settlement and restructuring of a company. This work is consistent with European Union’s “second chance” politics.
Tab. 1. Bankruptcy decisions in Poland in 2008–2013 according to Coface Polish Bankruptcy Information

<table>
<thead>
<tr>
<th>Type of bankruptcy proceedings</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bankruptcies to liquidate assets</td>
<td>348</td>
<td>572</td>
<td>538</td>
<td>620</td>
<td>711</td>
<td>718</td>
</tr>
<tr>
<td>Bankruptcies with possibility to enter into arrangement</td>
<td>63</td>
<td>119</td>
<td>117</td>
<td>103</td>
<td>166</td>
<td>165</td>
</tr>
<tr>
<td>Total</td>
<td>411</td>
<td>691</td>
<td>655</td>
<td>723</td>
<td>877</td>
<td>883</td>
</tr>
</tbody>
</table>


Most enterprises for which the court has declared bankruptcy in recent years in Poland, are enterprises from the SME sector (Tab. 2).

Tab. 2. Bankruptcies by legal form of enterprises

<table>
<thead>
<tr>
<th>legal form</th>
<th>number of bankruptcies 2011</th>
<th>number of bankruptcies 2012</th>
<th>number of bankruptcies 2013</th>
<th>change 2013/2012</th>
<th>share in 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Limited liability company</td>
<td>475</td>
<td>502</td>
<td>524</td>
<td>+4%</td>
<td>59.3%</td>
</tr>
<tr>
<td>Entrepreneur</td>
<td>133</td>
<td>210</td>
<td>204</td>
<td>-3%</td>
<td>23.1%</td>
</tr>
<tr>
<td>Joint stock company</td>
<td>52</td>
<td>81</td>
<td>76</td>
<td>decrease</td>
<td>8.6%</td>
</tr>
<tr>
<td>Registered partnership</td>
<td>29</td>
<td>45</td>
<td>37</td>
<td>decrease</td>
<td>4.2%</td>
</tr>
<tr>
<td>Limited partnership</td>
<td>12</td>
<td>16</td>
<td>20</td>
<td>increase</td>
<td>2.3%</td>
</tr>
<tr>
<td>Cooperative</td>
<td>18</td>
<td>20</td>
<td>15</td>
<td>decrease</td>
<td>1.7%</td>
</tr>
<tr>
<td>Other forms</td>
<td>4</td>
<td>3</td>
<td>7</td>
<td>increase</td>
<td>0.8%</td>
</tr>
<tr>
<td>total</td>
<td>723</td>
<td>877</td>
<td>883</td>
<td>+1%</td>
<td>100%</td>
</tr>
</tbody>
</table>


However, statistics confirm that, within a group of companies which are undergoing bankruptcy proceedings, joint stock companies still experience problems (nearly 9% of the total number of bankruptcies). Although, in accordance to Coface Report (2014, p. 7-8) their number slightly dropped, and in 2013 there were not as many companies listed on the Warsaw Stock Exchange among them as in 2012. The first seven places of the bankruptcy list in 2013 (in terms of turnover) are held by joint stock companies with arrangement bankruptcy declarations:

- Mix Electronics S.A.
- IDEON S.A.
- NOMI S.A.
- FOTA S.A.
- Energomontaż-Południe S.A.
- VISTALEX S.A.
- PIECEXPORT-PIECBUD S.A.

It is worth to mention here that among the largest companies, with turnover of more than PLN 100 million, bankruptcy with a possibility to make an arrangement is declared in nearly a half of the cases of all bankruptcies declared in this group.

In accordance with The Polish Bankruptcy and Reorganization Law the decision about the type of bankruptcy proceedings is not final and may change during the proceedings. This was true in the case of the following companies: Energomontaż-Południe S.A. and VISTALEX S.A. In the case of companies listed on the stock market, changing bankruptcy proceedings to liquidation of assets of an insolvent debtor leads to – after 6 months following the day of validation of the court’s decision – termination of disclosure obligations and withdrawal of the company's shares from trading on the regulated market.
4.2 Informative role of financial statements during bankruptcy proceedings which lead to an arrangement

Execution of bankruptcy proceedings which lead to an arrangement will affect financial data in a financial statement by:

- generating bankruptcy proceedings costs,
- usually leads to the sale of some assets to cover liabilities (including fixed assets intended for sale),
- can lead to the change of asset appraisal method (if continuation of business operations is threatened),
- results in the creation of reserves intended for restructuring.

The duty of an individual who draws up a financial statement is also to determine whether the risk of losing the ability to continue business operations is high and to include this information in the introduction of the financial statement.

Reporting obligations of an entity which is undergoing bankruptcy proceedings with a possibility to make an arrangement are regulated by the balance sheet law as well as the insolvency law.

The Polish Bankruptcy and Reorganization Law (art. 23) requires that an enterprise at risk of bankruptcy to file in court – along with declaration for bankruptcy – selected parts of a financial statement:

- a balance sheet drawn up for the purpose of these proceedings, valid as at the day falling no earlier than 30 days prior to the day of filing the petition,
- if the debtor applies for a declaration of bankruptcy with a possibility to make an arrangement also cash flow report for the previous 12 months (if the debtor was required to keep the records necessary to prepare cash flow report).

Moreover, after declaring bankruptcy, in the case of bankruptcy with a possibility to make an arrangement, a financial statement is drawn up for the day preceding the declaration of bankruptcy.

Besides the requirements of The Bankruptcy and Reorganization Law, a business owner is subject to accounting regulations. It is worth to note that, in the case of bankruptcy proceedings with a possibility to make an arrangement, a business owner has the same responsibilities coming from The Accounting Act, as he had during business operations before bankruptcy had been declared. In practice this means that, a business owner must draw up a financial statement and – if the law requires it – have it audited.

Information coming from reports can have a significant effect on early detection of a crisis. Data from financial statements is the base for creating early-detection models which can warn against bankruptcy, and can be applied in Poland as well as the rest of the world. Research confirms that financial statements are used during bankruptcy proceedings in many countries (Smith, Strömberg, 2004). However, research conducted in Poland confirms that, there are problems with the quality of financial information that could serve as a basis for assessment of the going concern risk (Wędzki, 2012).

Analysis of documents of enterprises undergoing bankruptcy proceedings confirm the existence of errors and inaccuracies in their financial statements (e.g. Dyczkowska, 2009, p. 6–8; Bauer, 2014, p. 652–666).

Concurrently, as Dyczkowska states (2009, p. 6): “a careful analysis of individual parts of a company’s financial statement can be significant for external users, who do not posses other reliable sources of information besides financial statements”.

The financial statement of an enterprise undergoing bankruptcy proceedings can also be a valuable source of information which can aid the bankruptcy proceedings and help to assess the possibility for the proceedings to be carried out by court representatives.

The Polish Bankruptcy and Reorganization Law regards the balance sheet as the most important part of a financial statement, which is submitted to court along with the request to declare bankruptcy. The balance sheet is the source of information about the value of assets which can
indicate whether or not it will be possible to carry out bankruptcy proceedings and satisfy creditors’ claims.

Moreover, the balance sheet is the basis for finding one of the conditions of bankruptcy (the sum of debtor’s obligations exceeds the value of his assets). In the case of bankruptcy proceedings with the intent to make an arrangement, the debtor must also submit to court a cash flow statement. Data from this statement is a valuable source of information when evaluating the ability to continue business operations. A cash flow statement provides information as to how much cash in the year preceding the submission of bankruptcy declaration came from business operations or, for instance, from asset liquidation. In turn, the introduction to a financial statement gives information as to whether it was drawn up under going concern assumption and whether there are circumstances indicating a threat to the continuation of business operations. Additional information includes necessary explanations to interpret data included in the remaining parts of a financial statement (more on this topic Bauer, 2009, p. 55–76).

Particular attention should be paid to the informative role of the commentary made by the board. The management report is one form of financial reporting that helps to interpret all parts of a financial statement and helps stakeholders to make decisions. An entity has the possibility of presenting additional disclosures in the board’s commentary and in doing so gain trust of the readers and users of this information. For this reason, it is crucial to identify what information is relevant (Krasodomska, 2014, p. 134). In accordance with The Accounting Act, art. 49 (The Accounting Act, p. 131) “the management report should cover material information on the property and financial standing, including an assessment of the performance as well as identifying any risk and threats”. In relation to the risk of bankruptcy, the management report should cover information about events having a material influence on the undertaking’s activity, which occurred both during the financial year and after its end, until the approval of the financial statements. It is worth to show in the management report information about expected development of the undertaking as a result of restructuring proceeding.

Individual parts of a consolidated financial statement should display information about bankruptcy proceedings which are in progress and may be beneficial to the users of the statement. Bankruptcy proceedings with the intent to make an arrangement increase the threat of losing the ability to continue business operations and makes estimates questionable. In addition, it can change the value and allocation of assets, cause the formation of restructuring reserves and generate legal fees. A consolidated financial statement of a group of companies should reflect this information. Above all, however, a consolidated financial statement should include information about the existence of bankruptcy proceedings as this is a significant event affecting the situation of the group of companies.

5. DISCLOSURE PRACTICE IN REFERENCE TO BANKRUPTCY WITH A POSSIBILTY TO MAKE AN ARRANGEMENT AS SHOWN IN CONSOLIDATED FINANCIAL STATEMENTS OF STOCK MARKET LISTED COMPANIES

5.1 Objective and research method

The objective of the study is to analyze the range of information on bankruptcy proceedings with a possibility to make an arrangement provided in consolidated financial statements of companies listed on the Warsaw Stock Exchange.

The results of the analysis will be examined in the context of consolidated financial statements as a source of information for external users.

The applied research method was an in-depth case study. Consolidated financial statements of 2 groups of companies whose shares are listed on the Warsaw Stock Exchange: IDEON S.A. and FOTA S.A., have been analyzed. Bankruptcy proceedings with the intent to make an arrangement were declared in 2013 in parent companies of those groups of companies.
Due to the date of announcement of bankruptcy, 2013 mid-year, third quarter and yearly consolidated financial statements were analyzed. In both cases, the mid-year statements were drawn up for periods during which the companies filed for bankruptcy. The third quarter and yearly statements refer to periods during bankruptcy proceedings.

Disclosures, which stem from the theory and practice of bankruptcy proceedings and which have an impact on the information contained in the financial statements, have been analyzed.

5.2 IDEON S.A.

5.2.1 General information

(ftp://ideon.eu/, date: 01.08.2014)

Ideon SA is a company acting in the Polish and Central Europe energy markets, and:
- is a participant of transactions in the wholesale market,
- participates in CO2 emissions trading,
- provides customers with specialized energy audits,
- participates in production of energy and heat,
- supplies biomass to power plants and thermal power plants.

Ideon SA Capital Group consists of companies actively involved in business activities in the energy market. It is a legal successor of Centrozap SA, former state foreign trade company founded in 1951, which it has executed a huge number of commercial contracts in the world's largest markets. Ideon SA employs experienced specialists with adequate qualifications allowing for smooth realization of contracts and services. The company possesses quality certificates and licenses authorizing performance of undertaken commitments. Ideon SA shares are listed on the Warsaw Stock Exchange.

The following units are included in IDEON Capital Group:
- PEC Śrem S.A. in Śrem (100% shares)
- WoodinterKom GmbH in Vienna, Austria (50.92% shares)
- Komi Pellet Sp. z o.o. (formerly CentroBudKom Sp. z o.o.) a company seated in Syktyvkar in Komi Republic, Russian Federation (indirect subsidiary)
- Ideon Real Estate Sp. z o.o. in Katowice (100% shares)
- Idea – Fix Sp.z o.o. in Katowice (100% shares)

On April 3, 2013 Ideon S.A. filed for bankruptcy with a possibility to make an arrangement. On August 8, creditors accepted the arrangement proposal. On September 4 the court declared bankruptcy with a possibility to make an arrangement and approved an arrangement with the creditors. On October 22, the court approved the end of bankruptcy proceeding with a possibility to make an arrangement in Ideon S.A.

5.2.2 An analysis of financial statements for information about bankruptcy proceedings with a possibility to make an arrangement

Consolidated financial statements of Ideon S.A. Capital Group included information about:
- filed petition to declare bankruptcy,
- prepared arrangement proposals,
- made arrangements,
- declared bankruptcy, court-approved arrangements,
- concluded bankruptcy proceedings.

Uncertainty of estimates, being the result of conducted bankruptcy with a possibility to make an arrangement, contributed to changes in the value of assets such as receivables and financial assets.
Bankruptcy proceedings also had other effects, such as: changing lease agreements to rental agreements.

In relation to reserves, only the third quarter statement included information that “in the analyzed period, there was no provision for restructuring costs”.

### Tab. 3. Results of an analysis of consolidated financial statements of Ideon S.A. Capital Group

<table>
<thead>
<tr>
<th>Disclosures on insolvency proceedings</th>
<th>The period of financial statements</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>possibility of a substantial doubt about an entity’s ability to continue as a going concern</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>declaration of bankruptcy—a significant event affecting the company's activities</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>uncertainty of estimates</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>updating of asset values</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>assets held for sale</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>restructuring in insolvency proceedings</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>provisions on restructuring</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>restructuring costs</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>costs of insolvency proceedings</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: own study

To sum up, in consolidated financial statements of Ideon S.A Capital Group information about ongoing proceedings and a substantial doubt about an entity’s ability to continue as a going concern has been disclosed. A lot of detailed information about ongoing bankruptcy proceedings is included in the management report (to mid-year and yearly statements) and in additional information (quarterly statements). No financial data connected to the ongoing bankruptcy proceedings has been supplied, that is bankruptcy proceedings costs and ongoing bankruptcy restructuring costs. Due to the amount of total assets and annual turnover, these values can be regarded as irrelevant.

### 5.3 FOTA S.A. in arrangement procedure

#### 5.3.1 General information (http://www.fota.pl/en/company/, date: 01.08.2014)

FOTA S.A. with its history dating back to the 70s of the previous century is a leading Polish distributor of spare parts for passenger cars, delivery cars and trucks as well as workshop equipment. Fota S.A. cooperates with about 200 business partners including several reputable manufacturers like: Bosch, ZF, SKF, ATE, MANN-HUMMEL, Federal Mogul. The company sells its own brands: KAGER, RACER (spare parts) as well as PDTools (workshop equipment, workshop tools).

Currently, they have a leading distribution network with a modern logistic centre in Łódź, several regional warehouses and almost a hundred sales points all over the country. Since 2001, the company has been operating a network of independent workshops under the name Leader Service and
Leader Service Truck associating nearly 400 partners. As part of the cooperation, the company offer business consulting services, supplies the network members with all the necessary spare parts, workshop equipment and workshop tools as well as provides training sessions for both garage owners and selected employees. FOTA S.A. shares are listed on the Warsaw Stock Exchange.

Fota S.A. in arrangement procedure with premises in Gdynia is the dominant unit within Fota Capital Group. Fota S.A. Capital Group has existed since 2005. The following units are included in Fota S.A. Capital Group:

- Art-Gum with its registered office in Mazańcowice (75.6% shares)
- Autoprima Slovakia with its registered office in Nitra (100% shares)
- Expom with its registered office in Kwidzyn (99.5% shares)
- Fota Ukraine with its registered office in Kiev (70% shares)

On 28 June, 2013 the board of Fota S.A. on behalf of the company, has filed for bankruptcy with a possibility to make an arrangement. On 12 September, the court has declared bankruptcy with a possibility to make an arrangement. Polish media have reported that upon declaring bankruptcy the company started “a deep restructuring”, which should be reflected in the results displayed in the financial statements.

5.3.2 An analysis of financial statements for information about bankruptcy proceedings with a possibility to make an arrangement

Consolidated financial statements of FOTA S.A. Capital Group listed on the primary market of the Warsaw Stock Exchange have been analyzed. The synthetic results are shown in Table 4.

Tab. 4. Results of an analysis of consolidated financial statements of FOTO S.A. Capital Group

<table>
<thead>
<tr>
<th>Disclosures on insolvency proceedings</th>
<th>The period of financial statements</th>
<th>comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>possibility of a substantial doubt about an entity’s ability to continue as a going concern</td>
<td>+</td>
<td>-</td>
</tr>
<tr>
<td>declaration of bankruptcy - a significant event affecting the company’s activities</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>uncertainty of estimates</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>updating of asset values</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>assets held for sale</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>restructuring in insolvency proceedings</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>provisions on restructuring</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>restructuring costs</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>costs of insolvency proceedings</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: own study
Consolidated financial statements of FOTO S.A. Capital Group contain many references to the bankruptcy proceedings relating to:
- filed petition to declare bankruptcy,
- planned and ongoing restructuring,
- declared bankruptcy.

The consolidated financial statements also included information about ongoing bankruptcy proceedings in companies in which FOTO S.A. holds shares.

In addition, risks associated with bankruptcy proceedings with the intent to make an arrangement have been described in the financial statements.

Particularly noteworthy is that, a substantial doubt about an entity’s ability to continue as a going concern is clearly emphasized only in the mid-year statement. The statement includes information that further business operations depend on the court’s decision and will be possible after the court declares bankruptcy with a possibility to make an arrangement.

No financial data connected to the bankruptcy proceedings and specific amounts relating to restructuring costs have been supplied. Due to the amount of total assets and annual turnover, these values can be regarded as irrelevant.

6. CONCLUSIONS

In Poland, the practice of bankruptcy proceedings is a relatively new phenomenon. Currently, amendments to The Bankruptcy and Reorganization Law are being worked on. The amendments are intended to facilitate the restructuring of indebted companies, and limit liquidation processes to companies that are not able to overcome the difficulties. At the same time, these changes are supposed to lead to transformation of bankruptcy proceedings from a law court procedure into a part of the economic process (Płoch et al., 2013). Along with work on amendments to the law, theoretical concepts are being created concerning the proposed changes to financial reporting of entities undergoing bankruptcy proceedings to make economic content more predominant over current precautionary and commensurate practices (Walińska, Jędrzejewski, 2009, p. 165–176), and to put focus on the way financial data is presented, for example bankruptcy proceedings costs (e.g. Chłodnicka, 2007; Sojak, Trojanek, 2010; Tokarski 2013).

In the case of stock market listed companies, the possibility of obtaining data on the risk of bankruptcy is particularly important, as they acquire funds from external investors. Investors expect full information on the risks associated with their securities. Therefore, it is advisable that in the event of bankruptcy proceedings with the intent to make an arrangement, a company which is part of a group of companies provides transparent consolidated financial statements. An analysis of the consolidated financial statements of the companies surveyed has indicated that they contain information on conducted bankruptcy with a possibility to make an arrangement. No information has been provided about bankruptcy proceedings costs or costs of restructuring at bankruptcy. However, they can be considered as a useful source of information to investors about the ongoing bankruptcy proceedings.

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IMPORTANCE OF PROPERTY RIGHTS SYSTEM FOR MANAGEMENT PRACTICES

Lucie CVIKLOVÁ
Charles University
lucie.cviklova@yahoo.com

Abstract: Transfers of public assets to private owners in various economic sectors have been recognized as one of the primary sources of economic change according liberal and institutional perspectives. Proponents of institutional economics have argued that post-communist privatizations were not symmetrical to communist nationalizations and that for this reason it was not possible to conceptualize economic reforms in terms of the big bang claimed by liberals. Adherents of institutional economics have argued that post-communist transformations should be seen through the perspective of formal rules and informal constraints: while formal rules could be changed relatively quickly by political mechanisms, informal rules have been rooted in social habits and routines and they cannot be changed very quickly due to their ‘path dependency tendencies’. Put in another way, according to the institutional perspective, property is not considered to be a set of rights and duties resulting from ‘invisible hand of the market’, but it is explained through the perspective of a mutual configuration between property rights and informal social habits. The article reviews the institutional conceptualization of early post-communist property changes to provide a framework for the adoption of more differentiated and more current models for the elucidation of interdependence between currently ongoing privatization processes and management practices.

Key words: political capitalism, spontaneous privatization, institutional privatization, institutional approach, management practices

INTRODUCTION

Given the fact of several decades of evolution of the capitalist property rights system in Eastern and Central Europe, including the Czech Republic, as well as former and current privatization processes, reformulation of research objectives related to the transfer of public assets to private hands is called for (Lízal and Švejnar, 2002; Roland and Stiglitz, 2008). Put in another way, a complex understanding of privatization processes implies not only the interpretation of economic results and the structural contexts of distributive processes but also a careful analysis of their ideological roots.

More concretely, over the last twenty years of post-communist development there have competed two distinctive and in many aspects opposite strands of perspectives concerning the transfer of public goods to private hands and they have also played an important role in governmental policies. The first one builds predominantly on a theory of neoclassical or liberal approach to capitalism, the other on the theory of institutional approach and its various forms (Klusnoň, 1991; Mlkoch, 1996).

While the liberal approach has dominated political scenes in many post-communist countries including the former Czechoslovakia, it has been very often criticized for negligence of property rights issues as well as transaction costs of the economic operations (Čapek and Mertlík, 1996). Proponents of institutional economics have argued that post-communist privatizations were not symmetrical to communist nationalizations and that for this reason it was not possible to conceptualize economic reforms in terms of the big bang claimed by liberals (Dembinski, 1995; Havel, 1997). Adherents of institutional economics have argued that post-communist transformations should be seen through the perspective of formal rules and informal constraints:
while formal rules could be changed relatively quickly by political mechanisms, informal rules have been rooted in social habits and routines and they cannot be changed very quickly due to their ‘path dependency tendencies’ (Stark, 1996; Šumpíková, 1999). 

Put in another way, according to the institutional perspective, property is not considered to be a set of rights and duties resulting from the ‘invisible hand of the market’, but it is explained through the perspective of a mutual configuration between property rights and informal social habits. The interdependence between distribution of property rights and privatization processes has particularly enabled better understanding of the redistribution of the state resources into private hands that had occurred in the framework of Eastern and Central European privatizations.

While neoclassical economists do not differentiate between the early privatizations and the current ones, according to proponents of the institutional approach the current privatization processes in Eastern and Central Europe are more close to those that had been realized in Western European Countries under consolidated capitalist conditions.

According to the institutional approach, early post-communist privatizations merged with distribution of properties in the framework of restitution programs, small and voucher privatizations, and they were more influenced by customary law than by written law. To put it more concretely, early post-communist privatization programs were ‘path dependent’ on the former socialist practices under which real property rights had been executed by a coalition of managers at the enterprise level who had negotiated with the formal representatives of the State Planning Commission (Palda, 1997). This approach suggests that in a similar way to the ‘socialist planning machine’ characteristic of socialist economies, the first post-communist privatizations were marked by the persistence of adaptation mechanisms that have played an important role for system equilibrium.

‘November 1989 paradoxically brought to these enterprise “bulls” more freedoms. Top management (directors) was very often changed, but middle management stayed and had to stay because there was nobody to replace it (in rare cases completely changed middle managements behaved in the same way as previous one: exceptions should not be denied). Control of enterprises – from the point of view of realization of any property rights – became anarchical; nevertheless enterprises did not collapse again and with different types of rapidity and intensity usually started to adapt at new circumstances.’ (Havel, 1997, p. 12).

OBJECTIVES AND METHODS

This article builds on the notion of ‘political capitalism’ and aims at differentiating between the early post-communist privatizations and the current ones: it frames current privatization strategies as a result of globalization and a source of revival of economics. By defining the crucial elements of the institutional approach to property changes and differentiating between ‘spontaneous’ and ‘institutional’ privatizations, the article arrives at a model facilitating a deeper insight and thus a better understanding and application of the notion of property rights and privatizations to the current property transfers of the state assets to new private owners.

RESULTS AND DISCUSSION

The most important proponents of the institutional approach claimed that the property system has been based on institutions and organizations: the former ones are determined by the rules of the game and the latter ones by their objective functions. Rules of the game have been particularly important for the execution of property rights by means of social habits and routines in those systems where conflict situations have usually been resolved by customary rules than by the written law (North, 1990).
Through the institutional perspective in almost all historical periods the property rights were executed only by the narrow elites and various interest groups – implied in their redistribution – according to their legislative power made attempts to change the rules of game in their own interest and for the sake of maximizing their material wealth.

‘Institutional privatization’, ‘spontaneous privatization’ and ‘political capitalism’ (the latter coined by Polish researcher Jadwiga Staniszkis) have been considered to be three crucial notions which could contribute to a deeper understanding of the continuities concerning everyday social routines and habits implied not only in the early privatization processes but also in the current ones. ‘Spontaneous privatizations’ occurred in Eastern and Central Europe, as well as the wider developing world, and they refer to the specific property transfer of material assets from state structures into private hands that occurred after the fall of the communist regimes in Eastern and Central Europe, as well as in developing countries, and that were realized by the former nomenclature cadres and operators.

In other words, the conceptual differentiation between ‘spontaneous privatizations’ and ‘institutional privatizations’ highlights the fact that certain types of property changes have emerged in rudimentary institutional conditions without distinction among individual, private and state property and without corresponding legal and social norms concerning the separation of individual, private and state ownership (Dembinski 1995). ‘Institutional privatizations’ occurred in the former Eastern and Central European countries, as well as in the Western ones, where their course was determined by respective privatization laws, decrees and regulations.

It is particularly thanks to the notion of ‘political capitalism’ that one can understand why Polish, Hungarian and Russian cadres realized large property transfers by means of ‘spontaneous privatizations’ and why, in the former Czechoslovakia, ‘spontaneous privatizations’ and ‘institutional privatizations’ occurred simultaneously and only after the fall of the socialist regimes in 1990. While in the western European countries differentiated regulations concerning ‘institutional privatizations’ prohibited the merger of economic and political interests by means of strict requirements for participation in respective privatization bodies, the deficiencies of the early Eastern and Central European privatizations were determined by several components.

Firstly, an institutional vacuum was brought about by the loss of legitimacy of many former socialist institutions; secondly, there survived informal constraints that could be conceptualized as modification of the former socialist habits and routines; and, thirdly, there occurred collective efforts to renew a pre-socialist institutional framework idealizing the institution of private property. In spite of formal public access to the submission of privatization proposals, only the coalitions of managers and insiders held necessary information concerning their formulation: for the sake of their interests they negotiated with the officials at the Ministry for Privatization and the Administration of National Property, similarly to their former communications at the State Planning Commission. Thus the importance of the survival of social routines and habits stressed by the institutional approach and its variation can be demonstrated by the success of those insiders who managed to submit several proposals concerning the same object and pretended that they were representatives of the company limited by guarantee.

According to Jadwiga Staniszkis’s concept of ‘political capitalism’, several factors have been identified which have been relevant for the differentiation between the distribution of property rights and privatization processes that has been crucial for a deeper understanding of early Eastern and Central European privatizations (Staniszkis, 1999). Despite the common structural features of distribution of property rights in the individual countries, the concrete national systems in Eastern and Central Europe came through three elementary stages of ‘political capitalism’ at different decades either under the socialist regime or only after its fall in 1989.

(1) First stage: disarticulation of the socialist means of production and temporary coexistence of various components of the old system with the new one (Hungary, Poland, Russia before 1989, the former Czechoslovakia only after 1989)
(2) First stage: establishment of new ‘satellites’ or ‘appendices’ parallel to the state enterprise where one director was not only at the head of the original state enterprise but also became owner or representative of the newly established component of parallel economy (Hungary, Poland, Russia before 1989, the former Czechoslovakia only after 1989)

(3) First stage: divided ownership under which managers or employees claim property rights concerning the same material objects (Hungary, Poland, Russia before 1989, the former Czechoslovakia only after 1989)

(4) First stage: uncontrolled merger or symbiotic existence of the private and public components as the result of the establishment of the private sector as well as privatization processes (Hungary, Poland, Russia before 1989, the former Czechoslovakia only after 1989)

(5) First stage: emergence of new forms of collective ownership by means of the privatization of political and social organizations through commercialization having been mostly realized by managers through governmental and party structures (Cviklová, 2008) that in some countries occurred simultaneously with ‘institutional privatizations’ (Hungary, Poland, Russia before 1989, the former Czechoslovakia only after 1989)

(6) Second stage: insufficient separation of the economic and political interests of the actors implied in the ‘institutional privatization processes: for example, in the Czech Republic decrees issued by a minister for privatization empowered the local representatives of Civic Forum, while other actors simultaneously occupied important positions in the party structures which coined privatization processes and in the state bodies responsible for privatization processes (only after 1989)

(7) Second stage: merger between real political and economic power structures. For example in Poland there was established the Agency for Economic Development [Agencja Rozwoju Gospodarczego] collecting state participation in many hybrid societies for the sake of the concentration and mobilization of capital. In the Czech Republic there occurred mergers of competences among the Ministry for Privatization, the Fund of National Property, the Consolidation Bank, as well as privatization funds which aimed at the administration of assets to former Czechoslovakian citizens by means of coupon privatization (only after 1989)

(8) Second stage: temporary anomic at the enterprise level brought about by non-transparent institutional conditions that can be explained by lack of execution of property rights in concrete enterprises, these processes were also relevant for agriculture (Hudečková, 1995; Petřáňová, 1997; Stryan, 1993) which was to large degree determined by restitution processes and transformation of former socialist cooperatives in new cooperatives of owners (only after 1989)

(9) Second stage: dysfunctions of the banking sector. For example the former Czechoslovakian government before 1997 was reluctant to put through bankruptcies necessary for the revival of the economic system: during privatization processes the state authorities and top banking managers permitted dysfunctional enterprises to receive loans, and in some cases even considered forgiving the loans of such indebted enterprises (Cviklová, 2002)

(10) Third stage: concentration and organization of capital and adaptation to the market structures for the sake of efficient competition with capital in more advanced countries. In the Czech Republic the third wave of privatization processes led to the centralization of formerly dispersed property and to the later constitution of real dominant property groups where the functioning of new capital was complicated by its concentration as well as by unreliable price indicators of the markets.
(11) Second and third stage: deficiencies of the legal framework (insufficient enforcement of law), which in the case of many enterprises brought about negative destruction or tunneling where the dominant owners established satellites in order to transfer profits as well as other assets to their own accounts.

Notions of ‘institutional’ and ‘spontaneous’ privatizations and ‘political capitalism’ have enabled us to explain the transfer of state assets into private hands that occurred in rudimentary transitional conditions parallel to the establishment of a capitalist property system and were influenced by the personal continuities of former nomenklatura cadres (Appel and Gould, 2000; Cviklová, 2008; Schutte 2000). ‘Political capitalism’ could be considered a variation of the ‘path dependency’ approach which takes into account the past heritage of concrete societies. On the basis of the perspective of ‘path dependency’, economic and political transformation is a recombination of institutional and organizational resources that have survived on the ruins of the former regime. Similarly to Staniszkis’s, Stark’s methodology comes out of the similarities between socialist past and capitalist present: under the socialist system there had existed a contradiction between hierarchically prescribed modes of action on the one hand and reciprocities and market transactions resulting from efforts to deal with economic system on the other. Similarly to Stark’s explanation of the Hungarian post-communist condition, several Czech authors have analyzed the phenomenon of cross ownership in the Czech Republic: cross ownership has not been established only among individual enterprises but also among key financial institutions (Palda, 1997).

Despite the fact that certain authors have stressed the importance of the past for the current condition (Lízal and Švejnar, 2002), current consolidated market structures and transformation of elites (Belke a Schneider, 2004; Berne a Pogorel, 2004; Engerer, 2001; Fungácová, 2009; Grahovač, 2001; Hodge, 2006; Knieps, 2004; Posuney, 2002; Roland a Stiglitz, 2008) call for the constitution of such a normative model that would not take into consideration only contradictions between rules of the game and informal constraints, but also advance an institutional framework under the consolidated market structures.

(1) Jurisprudence in the field of European law that would reflect upon the fact that frontiers between national and European regulations concerning transfers of state assets to private owners have been blurred: for example, national privatizations of fields such as telecommunication were interconnected with the continuous deregulation of the field.

(2) Conceptual differentiation of various transfers of public assets to private hands (Guislain, 1995): privatizations (they do not automatically bring diminution of state importance in the economic system, see Figure 1), denationalizations (they are retroactive processes to formerly realized nationalizations and ignore concrete forms of ownership, see Figure 1) and reprivatizations (they fully or partially give back expropriated properties to original owners or to their inheritors, see Figure 1).

(3) Respective norms such as directives, decrees and laws which should pay sufficient attention to the legal past of assets to be transferred: assets which were always owned by state structures (see field 1 in the Figure 1), assets which were not nationalized and were transformed into cooperatives (see field 2 in the Figure 1), assets which had been owned by cooperatives and only later on were nationalized (see field 3 in the Figure 1), assets which were collectively owned by cooperatives (see field 4 in the Figure 1), assets which were denationalized and which are about to be transformed into cooperatives (see field 5 in the Figure 1).

(4) Approach to concrete privatization waves including a schedule which would adopt a systematic approach to assets to be transferred: it could also imply the enumeration of concrete enterprises/agricultural cooperatives or classification of their importance in the national economy (positive experience of two waves of French privatization processes).
(5) Constitution of such a privatization committee, or committees, which would have an autonomous statute vis-à-vis state structures and which would be recruited from responsible experts who determine fixation of prices, schedule concerning state control in the enterprise to be transferred etc. The committee, or committees, should be nominated for a concrete period of time and should be composed of exactly a limited number of experts on the basis of a strict selection procedure in order to prevent a conflict of personal interests concerning decision-making processes.

(6) Given the negative effects of cross-ownership (Stark, 1996) which have maintained indirect influence on state structures and which are also the result of ‘institutional’ privatization processes, one should strictly define the conditions for the acquisition of privatized assets, privatization funds and certain operations of the capital market: the measures should prevent the emergence of cross ownership among financial institutions, among enterprises themselves as well as among financial institutions and enterprises.

(7) Implementation of transparent national regulations favorable for small investors in various economic sectors which would promote dispersed ownership and particularly increase the number of small shareholders: the broader citizens’ participation could also be achieved by the dissemination of necessary information concerning accessibility of the capital market as well as by concrete possibilities of participation at transfers of public assets to private owners.

(8) Consideration of specificities related to privatizations of the banking sector given the positive experience of ‘more ancient member states of the European Union’ concerning the interdependence between privatization processes of the banks and the advancement of transnational operations. Nevertheless, privatization processes of the banks should differentiate the importance of the bank for the national economy (the most important ones versus the local ones) and should be realized under the direct control of the Commission for Privatization, the Security Commission, etc.

(9) Adoption of measures which would reflect upon the internationalization of capital markets and respective institutions such as the International Organization of Securities Commission (Bos, 2000). National measures should strive for the participation of a well-informed citizenry and prevent...
informational asymmetry (brought about by principal-agent reasons) which very often leads to the passive attitudes of shareholders towards their investments.

(10) Adoption of such regulations at the enterprise or cooperative level which would prevent the concentration of the enterprise ownership among managers and related economic elites: it is necessary to adopt such a privatization scheme that would induce employees of concrete enterprises or members of cooperatives to invest in shares of the enterprise where they have or had been working, to promote ‘faithful’ shareholders who have participated in several waves of privatization programs.

(11) Adoption of regulations limiting property rights and management competencies that would protect as well as promote economic and social rights of workers by means of provisions concerning wages and collective agreements of tripartite system; it is necessary to prevent concentration or merger of social and political power at hands of managers and trade union representatives.

CONCLUSIONS

The processes of share issue privatizations, asset sale privatizations, voucher privatizations and privatizations from below are being realized in various countries in the world and enormous amount of sectors has already been privatized, is being privatized or is being under the consideration; among others one can mention privatizations of electricity, telecommunications, prisons, aircraft, etc. At the European level in the countries with developed property systems – such as England, France, Germany and others – privatizations were implemented between the eighties and today. Post-communist privatizations merged with the introduction of the capitalist property system and property rights and there is interdependence among them and decline of former communist regimes; regardless of omnipresent path dependency effect each former socialist country opted for different timing and scale of the processes.

Models of transfers of public assets to private owners by various privatization methods offer researchers and experts a framework for reformulating and reconfiguring private and public domains in various economic sectors. The distribution of property rights realized by former nomenclature cadres and operators before and after the fall of communist regime in Eastern and Central European countries can be interpreted as an objective process of the distribution of property rights necessary for market structures (liberal perspective), while concepts of ‘spontaneous’ privatization or ‘tunneling’ highlight the importance of formal and informal constraints coined by the institutional approach.

Nevertheless, according to the conception of ‘political capitalism’, notions of the disarticulation of means of production and divided ownership have had only an explanatory force for transfers of the state assets into private hands that occurred in transitional economies: current Eastern and Central European privatization processes in the housing sector and other fields call for explanation according to different perspectives and demand elucidation by means of different variables:

– internalization of financial institutions, banking sectors and capital markets call for a harmonization of regulation in the field;
– introduce such concrete measures in various fields which would reflect upon the merger of national and European frameworks and constitute the double structure of regulations and respective bodies (commissions, etc.);
– adopt such strict separation of institutional competences that would be transparent to broader public structures and would prevent corrupt elements and the spread of semi-legal phenomena like cross-ownership or monopolization of privatized assets by local economic elites/managers (or eventually appropriation of assets by actors in the shadow economy);
– mobilize human potential – at the national level as well as at the level of management practices by the adoption of such measures which would attract new shareholders and at the same time prevent a constitution of concentrated ownership as well as collective protestations against privatization processes;
– mobilize human potential by means of management practices at the ‘grassroot’ level which would promote dispersed ownership at the enterprise/cooperative level or eventually in the housing sector by means of employees’ or tenants’ local investments.

| 1) | Publication of laws that would enable all parties concerned to become acquainted with laws that one should respect. |
| 2) | Clarity and reliability of legal framework that would enable to parties concerned to identify laws concerning their situation and determine their concrete meaning. |
| 3) | Predictability concerning legal rules that reduce risk related to changes concerning interpretation and application of laws. |
| 4) | Principle of non-discrimination concerning application of legal rules demands imposition of equal obligations to all parties that are in the same situation. |
| 5) | Provision of options concerning appeal and respect on the basis of planned procedure that would guarantee access to independent mechanisms of appeal and solution of legal dispute. |
| 6) | Stability of political and legal framework as well as decisions that would give investors security that state and government unilaterally and unfavorably won’t change basic conditions that have become basis for their decisions concerning investments. |

Fig. 2. Principles that guarantee the rule of law regarding privatization processes

BIBLIOGRAPHY


DIFFICULTIES IN THE IMPLEMENTATION OF AN ERP SYSTEM: EVIDENCE FROM A TRANSITION ECONOMY

Valentin Florentin DUMITRU
Bucharest University of Economic Studies
Valentin.Dumitru@cig.ase.ro

Abstract: Previous research on ERP systems (ERPSs) shows that the risk of failure is very important. Also, the difficulties in implementing an ERPS in a transition economy are different from the ones encountered in a developed country (Huang and Palvia, 2001; Roztocki and Weistroffer, 2008). Our research relies on the presentation of a case study developed in a Romanian company implementing an ERPS. Based on the literature review, we define the phases of the implementation process (Markus and Tanis, 2000; Parr and Shanks, 2000; Ross and Vitale, 2000; Somers and Nelson, 2004). In the literature review section we present as well the difficulties encountered by a company implementing an ERPS in a transition and in a developed economy in a comparative form. Our paper will continue with the presentation of the difficulties encountered in our case company. The implementation started in 2013 and difficulties related to financing, IT infrastructure, employees, management etc. were identified. We present the difficulties on specific implementation phases. Both authors were actively involved in the implementation process, which makes this paper an action research.

Keywords: difficulties, ERP systems, implementation phases, transition economy

1. INTRODUCTION

The emerging market economies are defined by a rapid increase of their GDP, even though it has a small value per capita as compared with developed countries (Roztocki & Weistroffer, 2009a). They are spread all over the globe and are divided into the following groups (Hoskisson et al., 2000): Latin America, East Asia, Africa/Middle East and Central and Eastern Europe. The transition economies represent a subgroup of emerging market economies located in Central and South-Eastern Europe and in the ex-Soviet Union that are moving from a central planning system to a market economy. They are confronted with plenty of problems, such as the lack of employment opportunities, the lack of infrastructure, poverty, frequent changes in regulations, high levels of corruption etc. Romania is a country in transition and this process started in 1989. In 2007 Romania joined the European Union. Our research goal is to investigate in order to avoid the difficulties which may arise in the implementation of an ERPS in a transition economy. We do this by presenting and discussing the difficulties encountered in the implementation process in a Romanian company.

The motivation of our research comes from the importance that we grant to the ERPSs adoption in transition economies. In these countries, ERPSs compensate the poor management systems and the lack of infrastructure. Also, IT systems are particularly important, as they support the business functions. The ERPSs adoption is more difficult in transition economies than in developed countries, as the environment in which the entities operate is constantly changing. Many failures were reported as these are very complex projects. It is important to discover issues influencing the implementation outcome.

Our paper is structured as it follows: after a presentation of the literature review on the difficulties signalled by other authors in the process of ERPSs implementation and on the phases of the implementation project, we present a section regarding the research methodology that we employed for this article, compared with the research methodology used by other authors. A section dedicated to the results of our study follows. Our paper ends with our discussion, conclusions and suggestions for future work.
2. LITERATURE REVIEW

There are many differences between ITC in developed and emerging countries (Roztwocki and Weitroffer, 2009a, 2009b): diffusion, security, strategy, economics, planning and design, users and organizations, implementation, services, management and sourcing. In this paper we present the difficulties identified in our case company during the implementation phases. Other studies identified the following phases (see table 1).

Tab. 1. Phases identified in the ERPSs implementation

<table>
<thead>
<tr>
<th>Article</th>
<th>Phases</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cooper and Zmud, 1990 (further analysed by Somers and Nelson, 2004)</td>
<td><strong>Initiation:</strong> Companies justify the need for adopting an ES system, choose the actual enterprise system, and define business needs and goals.</td>
</tr>
<tr>
<td></td>
<td><strong>Adoption:</strong> The definition of the project takes place and the model/design is created. Issues related to project management are investigated. Project participants are selected. Usually, the relationship between the client and the provider begins at this stage.</td>
</tr>
<tr>
<td></td>
<td><strong>Adaptation:</strong> This is the main implementation stage where the technical team translates the solution design into reality.</td>
</tr>
<tr>
<td></td>
<td><strong>Acceptance:</strong> The aim of this phase is to deliver and run the system.</td>
</tr>
<tr>
<td></td>
<td><strong>Routinization:</strong> This phase is part of the post-implementation phase.</td>
</tr>
<tr>
<td></td>
<td><strong>Infusion:</strong> This is the post-implementation period where the company experiences the full potential of the ES operation.</td>
</tr>
<tr>
<td>Soh and Markus, 1995 (redisussed by Kumar et al., 2003)</td>
<td><strong>IT expenditure:</strong> efficient acquisition of IT assets.</td>
</tr>
<tr>
<td></td>
<td><strong>IT assets:</strong> appropriate use of the assets.</td>
</tr>
<tr>
<td></td>
<td><strong>Organizational impacts:</strong> IT impacts and organizational performance.</td>
</tr>
<tr>
<td>Markus and Tanis, 2000</td>
<td><strong>Chartering:</strong> Decisions defining the business case and solution constraints making a key business decisions concerning the scope of the project, budgeting, choosing system vendor etc.</td>
</tr>
<tr>
<td></td>
<td><strong>Project:</strong> the main implementation phase with the purpose of getting system and users “up and running”.</td>
</tr>
<tr>
<td></td>
<td><strong>Shakedown:</strong> Stabilizing, eliminating ‘bugs,’ getting to normal operations.</td>
</tr>
<tr>
<td></td>
<td><strong>Onwards and upwards:</strong> Maintaining system, supporting users, getting results, upgrading.</td>
</tr>
<tr>
<td>Parr and Shanks, 2000</td>
<td><strong>Planning:</strong> developing the initial business case.</td>
</tr>
<tr>
<td></td>
<td><strong>Project:</strong> configuring and implementing the packaged software (Set up, Reengineering, Design, Configuration and testing, and Installation).</td>
</tr>
<tr>
<td></td>
<td><strong>Enhancement:</strong> subsequent improvements to business processes.</td>
</tr>
<tr>
<td>Ross and Vitale, 2000</td>
<td><strong>Design:</strong> decide on whether or not to accept the process assumptions embedded in the software and process customization.</td>
</tr>
<tr>
<td></td>
<td><strong>Implementation:</strong> the “go live”.</td>
</tr>
<tr>
<td></td>
<td><strong>Stabilization:</strong> processes and data clean up and adjusting to the new environment.</td>
</tr>
<tr>
<td></td>
<td><strong>Continuous improvement:</strong> adding functionality through new modules or buttons.</td>
</tr>
<tr>
<td></td>
<td><strong>Transformation:</strong> transformation of the company (e.g. changing organizational boundaries).</td>
</tr>
<tr>
<td>Esteves and Pastor, 1999</td>
<td><strong>Adoption decision phase:</strong> establishment of the need for the system, definition of system requirements, goals and benefits, analysis of the impact of adoption.</td>
</tr>
<tr>
<td></td>
<td><strong>Acquisition phase:</strong> product selection.</td>
</tr>
<tr>
<td></td>
<td><strong>Implementation phase:</strong> customization and adaptation of the ERP package.</td>
</tr>
<tr>
<td></td>
<td><strong>Use and maintenance:</strong> use and maintenance of the system in a way in which it brings the expected benefits.</td>
</tr>
<tr>
<td></td>
<td><strong>Evolution phase:</strong> integration of further capabilities into the system.</td>
</tr>
<tr>
<td></td>
<td><strong>Retirement phase:</strong> the decision of the manager to substitute the ERP.</td>
</tr>
</tbody>
</table>

Source: Compilation of the authors
In transition economies, another phase is identified, called “Decline” (Themistocleous et al., 2011). During this phase, the client decides on whether to continue or abort the project. In their work, Themistocleous et al. compare the opinions of consultants and adopters of locally developed ES from a transition economy (Poland) with the opinions of consultants and adopters of internationally recognized ES systems in a developed economy. We consider that the decline phase in the latter case doesn’t exist because of the type of ES adopted, not just because of the characteristics of the economy. In this paper we adopt the classification suggested by Cooper and Zmud (1990).

The adopters in developed countries and the adopters in emerging economies grant different importance to the phases. Thus, according to Themistocleous et al. (2011), the Polish tended to grant a bigger importance to “Initiation” and “Adoption”, while UK respondents considered more important the “Infusion” phase. The “Adaptation” and “Routinization” phases are less important for the Polish respondents than for the UK ones.

Most of the classifications mentioned above incorporate an initial phase and a post-implementation phase.

Soja (2010b) describes the adoption of enterprise systems in a transition country (Poland) as a *people-related project*. Also, some changes in time are observed, from difficulties connected with infrastructure and finance to human issues (Soja and Paliwoda-Pękosz, 2013).

The difficulties encountered when implementing an ERPS in a developed country are mostly business-related and appear in the project phase, while the differences in the transition economies are system-related and occur during all the lifecycle phases. ITC adoptions in transition economies face financial and employees-related difficulties, such as: lack of a well-set budget for the implementation, bad management systems that fail to set a strategy for the company and for the ITC project, difficulties related to various stakeholders (in terms of their education, experience, knowledge, attitude etc.), difficulties generated by the ITC infrastructure etc. (Soja and Paliwoda-Pękosz, 2013; Huang and Palvia, 2001; Roztocki and Weistroffer, 2008b). Various types of differences were identified by other authors, as it follows (see table 2).

<table>
<thead>
<tr>
<th>Article</th>
<th>Classification of difficulties</th>
</tr>
</thead>
<tbody>
<tr>
<td>Soja and Paliwoda-Pękosz, 2009</td>
<td>Categories of problems identified by enterprise systems adopters: employees, enterprise, system, IT infrastructure, system misfit, system replacement, training, implementation process, system vendor</td>
</tr>
<tr>
<td>Soja, 2008</td>
<td>Categories of problems identified by experts: economic, technical, organizational, social</td>
</tr>
<tr>
<td>Themistocleous et al., 2001</td>
<td>Managerial problems during and after ERP implementation: project cost overrun, project delays, conflicts with business strategy, employees resistance to change, conflicts with consultants, internal conflicts, conflicts with vendors Technical problems: integration with existing systems, customization, integration with other applications, European currency, security, other</td>
</tr>
<tr>
<td>Grossman and Walsh, 2004</td>
<td>Technical, operational and legal aspects</td>
</tr>
<tr>
<td>O’Leary, 2000</td>
<td>Companies: Budget over-run, time over-run, lack of benefit, meets or does not meet business plan criteria</td>
</tr>
<tr>
<td>Kim, Lee and Gosain, 2005</td>
<td>Critical impediments are from functional coordination problems related to inadequate support from functional units and coordination among functional units, the project management related to business process change, and change management related to resistance of users</td>
</tr>
<tr>
<td>Kremers and van Diesel, 2000</td>
<td>Problems encountered with migration of ERP systems from the point of view of the adopters: time needed for implementing the new version, technical problems with the new version, bad estimates by migration partner(s), costs involved, strain on the organization, quality of the migration support tools</td>
</tr>
</tbody>
</table>

Source: compiled by the authors
According to Soja (2008), the top five difficulties reported by the Polish experts are: employees’ knowledge and education, top management, high costs, project goals and implementation team. Other issues might be users’ responsibility and availability, company’s condition and stability, system’s efficiency. The difficulties from adopters’ perspective are system provider’s competence, system drawbacks and efficiency, inadequate project plan, infrastructure.

Previous studies identified the critical success factors (CSFs) for ERPSs adoption. Critical success factors represent the limited number of areas of enterprise activity in which the achievement of satisfactory results will ensure competitive performance for the organisation (Rockart, 1979). We argue that the same areas are the ones that can generate difficulties for the enterprise. For instance, Soja (2010a), based on a study conducted in Poland, identifies the following categories of CSFs for ERPSs adoption: employees, adoption participants, adoption project run, adoption preparation. The same study identifies CSFs not present among developed countries (employees’ attitudes, employees’ characteristics, cooperation, company’s condition, and visible benefits) and CSFs not declared by the Polish respondents (balanced team, IT infrastructure, managing cultural change, post-implementation evaluation, legacy system consideration, client consultation). The barriers declared only by the respondents in transition economies include reluctance, workload, attitude, people, system fit, culture, while the barriers declared only by the persons from developed countries are group coordination and pressure from the environment.

In this study we adopted the classification of the ERPS implementation phases suggested by Cooper and Zmud (1990) and the classification of the difficulties encountered suggested by Soja and Paliwoda-Pękosz (2009).

3. METHODOLOGY

Other studies related to the difficulties encountered in developed or emerging (transition) economies employed the following methodology (see table 3).

<table>
<thead>
<tr>
<th>Article</th>
<th>Research methodology</th>
</tr>
</thead>
<tbody>
<tr>
<td>Themistocleous et al., 2011</td>
<td>7 interviews with consultants and adopters from the Polish and UK companies</td>
</tr>
<tr>
<td>Soja and Paliwoda-Pękosz, 2013</td>
<td>Qualitative approach based on the grounded theory; 83 interviews with Polish ES practitioners</td>
</tr>
<tr>
<td>Soja, 2008</td>
<td>Questionnaires sent to 45 people and 31 (69%) experts’ opinions were gathered</td>
</tr>
<tr>
<td>Soja and Paliwoda-Pękosz, 2009</td>
<td>Grounded theory, semi-structured questionnaire, 82 opinions from respondents</td>
</tr>
<tr>
<td>Themistocleous et al., 2001</td>
<td>Questionnaires distributed on the Internet, 67 answers received, 50 questionnaires analysed</td>
</tr>
</tbody>
</table>

Source: compiled by the authors

In this article we present a case study on a Romanian company called here ABC. The sample company started to implement a Romanian ERPS in 2013. We want to present the difficulties encountered by this company during the deployment of the ERPS, on different phases. We base our study on a solid theoretical background.

In order to analyse the difficulties encountered by the company ABC, we interviewed the persons involved in the deployment process. The list of interviews is the following (see table 4).

Tab. 4. List of interviews

<table>
<thead>
<tr>
<th>Interviewee</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vendors’ selling agent</td>
<td>March, 2014, app. duration 90 minutes</td>
</tr>
<tr>
<td>Vendors’ project manager</td>
<td>March, 2014, app. duration 60 minutes</td>
</tr>
<tr>
<td>Vendors’ deployment consultant</td>
<td>March, 2014, app. duration 60 minutes</td>
</tr>
<tr>
<td>Adopter’s manager</td>
<td>April, 2014, app. duration 90 minutes</td>
</tr>
<tr>
<td>Adopter’s accountant</td>
<td>April, 2014, app. duration 60 minutes</td>
</tr>
</tbody>
</table>

Source: compilation of the authors

Other methods used for data collection were:
- Direct observation: the authors of this paper were members of the implementation team and as such they had the chance to notice directly the process;
- Financial statements;
- Internal reports.

Unlike other studies (e.g. Soja, 2008; Soja and Paliwoda-Pękosz, 2013), we benefited from the opinions of both the representatives of the ERPS vendor and the adopters.

4. CASE STUDY

The description of the research site and the motivation for implementing an ERPS

ABC is a reseller. It sells mostly parapharmaceutical products, organic and other plant-based products. The company employs 10 sales agents. The sales contact the drug stores directly or by telephone and take their orders. The orders are transmitted to the warehouses where a number of employees are preparing them. Most of the products are very cheap and one can easily make mistakes when selecting the products that the buyer wants. For instance, the lime tea boxes look almost the same, even though the prices are different. If the drug store receives a more expensive product and pays for a cheaper one, usually its employees don’t report on the mistake. It results that there are many problems with the inventories.

They have one central warehouse close to Bucharest and three other selling points in the most important geographic areas in Romania (Moldova, Banat, Ardeal). Before implementing the ERPS there was different software in each area for the management of the sales and cash. Also, there was accounting software in Bucharest which was used for the preparation of the statements required by the state. In total, a number of five software packages were running, which generated plenty of problems. The data from these software packages were exported in order to generate the statements required by the state. Yet, nobody was checking the data exported. As the accountant states, she was never certain that the figures communicated by the other selling points were correct. They never checked the real inventories, the amount of sales etc.

The company has an Accounting department in which works an accountant and her assistant. As such, the accountant is already overloaded. The company also has a contract with an accounting firm which is responsible for preparing the statements for the authorities. Another person who works in the Selling department is responsible for the payments and manages the customers’ lists.

The company has only one person working in the IT domain. He owns a little percentage of the company and is a Portuguese. He is not a fluent speaker of Romanian, and as such, he has difficulties in communicated with the other employees and with the other members of the implementation team. He also has problems to understand what other persons are telling him.

The difficulties encountered during the ERPS implementation and employment

During the Initiation phase, the vendor’s sales agent contacted the owner of the adopter. The first contact was established in 2011. Two/three presentations followed. As the adopter’s owner is saying, he told the vendor’s agent from the very beginning that it is going to be very difficult, but the agent was stubborn enough and never gave up. So, we consider that in this case, even though the adopter’s
representatives were aware of the problems they have within the company, they were not prepared to get engaged in such a process.

Difficulties encountered during the Adoption period were related with the establishment of the price for the ERPS and of the number of hours included in the initial price. As the adopter wanted to cut the prices, it had to cut the number of licences and/or the number of implementation hours. As such, they searched for alternative solutions which were not recommended by the vendor (for instance, they wanted to use for the selling points outside Bucharest remote desktop connections). Also, the contract signed by both parties included the characteristics of the system and the vendor specified several times that the ITC infrastructure available at the adopter’s headquarters was old and poor. From the point of view of the vendor’s selling agent, the adopter lacked a general and long term vision of the system. ERPS modules don’t function separately. If the user doesn’t have a full vision of the functionalities of the new system, there is a risk of errors in the implementation and the increase in the number of hours initially established. In addition, an employee who is aware of the processes will be able to help the vendor through a good cooperation and the supply of useful information for the system’s configuration.

According to the vendor’s representatives, the adopter didn’t establish any goals. If you don’t know what you want from an ERPS, no supplier will be able to help you. Abstract goals, such as “process optimization” or “activity’s improvement” are not useful. It is important to know exactly how is the ERP going to bring benefits to your business. For instance, goals such as “the increase of the inventories turnover by 20%” or “the reduction of the period for the invoices collection by 30%” can be formulated. These can be verified later, in the post-implementation phase.

In the Adaptation phase the employees of the adopter started to get involved. The system was customized. However, from the point of view of the vendor’s deployment consultant, the process didn’t go as smoothly as it should have, because nobody wanted to take any responsibility. The employees were confused because the ERPS brought changes in the way they were dealing with the processes and the management didn’t support the implementation (the top manager always had a joking attitude and never stepped in to help his employees understand the importance of the ERPS). Other problems encountered during this phase were with the import of data. As we stated above, the IT specialist was not speaking well Romanian, so he had troubles understanding what he was supposed to give to the vendor’s team. As such, the import was made several times, because each time problems were discovered. According to the vendor’s representatives, a failure in the implementation and employment of new software is to bring errors into the database. A functioning error can be easily identified and corrected, but the errors coming from the database make the system hard to be used. The solution is a careful verification of the information that is about to be introduced. The project team established that the implementation was supposed to start on July, 1st, 2014. However, the data was not ready on that date and the implementation started on July, 4th. This caused plenty of problems, as it was a lot more difficult to check the reports generated for the month of July. Another problem with the data introduced from the old system was the initial balances of the accounts. In the old system there were many errors, for instance several times the totals were not correct.

During the first month, the system broke down twice. From the point of view of the vendor, this was because of the adopter’s IT infrastructure. For instance, they did not use a server, but they had seven computers/users connected to the database. From the point of view of the adopter’s manager, he bought the system and he was expecting it to be ready to run within a day. Also, he did not plan to make further investments. As a consequence of the breakdown, data introduced in seven days was lost, which generated further problems with the employees. According to the vendor’s representatives, most of the times the customers don’t make an assessment of the hardware available before the implementation and the use of inadequate hardware or network breakdowns represent a source of problems along the project.

The employees which were the main users of the ERPS were overloaded with their daily tasks. So, it was very difficult for them to find time to learn the system. Yet, they had a positive attitude and never complained. They also knew the processes had to follow certain steps and it was difficult for them to understand that things can run better in a different way. For instance, the bank transactions
are checked by somebody in the selling department who communicates too late with the accountant. Many times they feel that even if they do things right, their colleagues won’t do them too and their effort will be in vain (for instance, the accountant considers that even though she will register the selling invoices correctly her colleagues won’t be able to verify them). Previously, they used very simple systems and it is difficult for them to use more complex software packages as they don’t feel any improvement in company’s operational performance and they are not rewarded. Also, the accountant considers that her assistant cannot perform certain tasks because she lack the knowledge. Yet, she never tried to let her assistant try.

In this case, the Acceptance phase overlapped the Adaptation phase. There was no testing period, so the system had to be prepared as the employees were already using it in order to perform their daily tasks. This brought plenty of difficulties, as the vendor’s team had to configure the system and train the persons in the same time. Many errors occurred and as such the vendor spent more time than it was originally planned. In the same time, employees lacked training in areas that they didn’t use on a daily basis because the vendor’s consultants had to deal with other issues during this phase.

The Routinization phase started in October, 2013. During this phase, there were still difficulties connected with the verification of the reports. The first statements were prepared using the new ERPS. The accountants were satisfied with the process. From the adopter’s manager point of view, the main issues with the system are that it doesn’t run quickly and that the vendor’s costs are too high. Yet, the vendor’s representatives consider that the management didn’t support the implementation, it doesn’t go to the real problems and that the adopter will always have problems without a good IT infrastructure.

In our opinion, the Infusion phase didn’t start yet. The ERPS was not introduced so far in all the selling points. So, the adopter is still experiencing a lot of the problems it had before the adoption of the ERPS. From the vendor’s point of view, there was a financing issue, as the adopter was not willing to purchase a server and make the system running at its potential.

5. CONCLUSIONS

We found the problems identified by Huang and Palvia (2001) in the developing countries, namely “(a) low IT maturity, (b) small firm size, which raises the issues of affordability and availability, and (c) lack of process management orientation and BPR experience.”

In this case study, there was no consultant. Most of the problems in our case study were generated by the top management. This is different from other studies, which report organizational issues as most important (Soja, 2008). The second source of difficulties was generated by the employees. They had bad habits and some of them didn’t have the necessary knowledge to perform their tasks. Also, because of the reduced number of training, they do not have the necessary skills, which lead to mistakes in operating the system. They are not motivated to use the system at its full capacity. Related to employees, in our case study we found two of the problems signalled by Nah et al. (2004): perceived ease of use and perceived usefulness.

The difficulties related to the enterprise are caused by the poor management system, which is a characteristic of the Romanian enterprises (Dumitru et al., 2012). The enterprise has financial problems, which leads to problems with the IT infrastructure.

The main difficulties identified by the vendor, especially by the vendor’s project manager relate with the IT infrastructure. In his opinion, it is old and the adopter has no intention to invest. The IT employee is incompetent and supplied incorrect data. The cause is the decision of the manager to have low costs, which in the end generates higher costs. The IT infrastructure is the cause of the system’s inefficiency, which is main concern of the manager.

We don’t consider that in this case there was a system misfit, as the system could be customized according to the adopter’s necessities. There were problems with the import of data, but they were connected with the IT employee of the adopter. Yet, the change occurred suddenly and this could generate problems for the adopter.
Regarding the training, the number dedicated to this process was not separately mentioned in the contract. Rather, there was a total number of hours dedicated to the “implementation,” including the system installation, the import of data, the configuration, training, verification etc. Unfortunately, because of the lack of organization from the management, several operations had to be done several times (for instance, installation of the system, import of data). Thus, the number of hours remaining was limited. The schedule did not cause any difficulties, as the vendor’s team went to the adopter when it was called.

The implementation process was not granted the importance required by the top manager. He didn’t realize how complex the process is and thus the project definition was very bad.

Finally, the system vendor had enough consultants and resources to support the project, but the bad definition and organization of the project affected its activity as well.

In this study we made an in-depth stakeholder analysis of the difficulties discovered from the point of view of various persons as we considered that all the opinions are important because of their involvement in the project run and the complexity of the implementation. Our study was conducted after the crisis and this could have an impact on the stakeholders’ attitude. Thus, even though the employees experienced most of the difficulties, they didn’t complain and they had a positive attitude related with the project. In the same time, the vendor agreed to negotiate the price and offered support even when the problems encountered were not caused by it.

Future research may present the analysis of several companies implementing and ERPS. Other research may have as a subject a comparison between the implementation and deployment of the projects in public sector entities, companies and not for profit organizations.

ACKNOWLEDGEMENT
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FINANCIAL REPORTING IN ACCORDANCE WITH IFRS—ESPECIALLY IAS 1 – REQUIREMENTS AND INTERNET FINANCIAL DISCLOSURE: THE CASE OF ROMANIAN LISTED COMPANIES

Ionelia-Alexandra FELDIOREANU
Ph.D. Student, Bucharest University of Economic Studies
alexandrafeldioreanu@yahoo.com

Abstract: The aim of this study is to analyze the Romanian listed companies with the disclosure requirements contained by IAS 1, by analysing the 2012 annual reports, but also the companies' websites. Secondly, the paper will try to analyze the association between the companies' disclosure quality and some internal variables, such as companies' size and the type of auditor. Results confirmed that entities audited by a Big 4 auditor comply to a higher extent the requirements of IFRS. The conducted study highlights the tendency of the size of the entities appear to influence the value of the disclosure index compliance with IFRS.

Keywords: Corporate governance, IAS 1, Performance disclosure, Romanian listed companies

1. INTRODUCTION

Compliance of financial statements with information requirements of international accounting referential is a complex issue addressed by many papers that require a prior knowledge of the way the recognition, measurement and presentation of all existing transactions in a society.

The purpose of this paper is to analyze the extent to which companies listed on the Bucharest Stock Exchange (BVB) comply with the information requirements of international reference. It is very important that the information provided to allow users to fully and correctly understand the reality that lies behind their preparation.

Given that 2012 is the first year that these companies are required to prepare financial statements in accordance with International Financial Reporting Standards, we considered useful to analyze the degree of disclosure of compliance requirements specified by IFRS. Unlike the Romanian accounting, which is a rule-based framework based on IFRS principles. The immediate benefit of companies that are part of international groups is the possibility of applying the Group's accounting policies (based on IFRS) accounting in Romanian, so we can say that this move was made to harmonize the statutory requirements and those of reporting to the group. All market players need transparent, consistent, comparable and complete decision making. Extending the scope of IFRS in Romania is the result of the agreement among Romania with the IMF and the European convergence process.

The benefits of applying IFRS in our country are many among which we can mention that will ensure comparability of information, increase transparency of financial information, reduce information asymmetry, attracting foreign investment and not least lowering the cost of capital.

2. A REVIEW OF THE LITERATURE AND STUDIES ON THE APPLICATION OF IFRS

Over time there have been many studies on financial reporting in which each researcher tried to bring their vision. Cuc and Kanya (2009) concluded that the financial statements and disclosures in general by listed companies have a greater degree of transparency.
According to a survey conducted by KPMG in 2010 the most important factor that can cause difficulties in the implementation of IFRS is the knowledge and technical skills of the staff, and the most important costs are those related to staff training and upgrading / purchasing software.

Ionașcu et al. (2011) investigates the benefits of implementing IFRS and institutional factors that influence the implementation process. As a result of the study is emphasized that CFOs believe that the adoption of IFRS has improved or will improve the quality of disclosure to investors, especially due to increased comparability and use of fair value. It is very important that the transparency of financial statements to be increased to attract investors and improve the capital market.

Gîrbină and Bunea (2009) examined compliance with IFRS 7 of the entities that have published an annual report in accordance with International Financial Reporting Standards and have concluded that the activity and structure of financing influence the degree of financial reporting on risks.

Albu and Guta (2013) conducted a study that analyzed the quality of information presented in the consolidated financial statements prepared under IFRS of companies listed on the BSE. The finding was that the level of transparency and communication is relatively good and growing from previous studies. They observed a high level of transparency in the reporting of the effects of new standards, the financial impact information, audit and last but not least, information about non-financial.

Financial statements prepared in accordance with national legislation are less credible to investors than those prepared in accordance with International Financial Reporting Standards. Even though Romania has tried to align with the EU provisions on accounting and auditing, investors prefer financial statements in accordance with IFRS and audited by Big 4 companies (PricewaterhouseCoopers, KPMG, Ernst & Young, DeloitteTohmatu & Touche). Following the studies reached the following conclusion: the larger a company is, the more it will post more information and better representing something that takes the image and reputation of the company and other entities in the same industry will try to keep up this level of information, or being perceived as companies that have something to hide to the users.

3. RESEARCH METHODOLOGY

3.1 Sample description and data sources

My study aims to discover to what extent companies listed in the first tier of the Bucharest Stock Exchange do comply with the requirements of IFRS, especially IAS 1.

The analysed sample is comprised of 16 non-financial companies, listed on the Bucharest Stock Exchange. For 2012, in the first category of BSE were listed 28 companies, of which 10 conduct financial activities. The latter were removed from the analysis because of the particularities of the type of the activity. I also removed other two companies that have been classified as Category I, after the year 2012, therefore, the study investigates the extent to which these companies disclose information required by International Financial Reporting Standard for all 16 companies listed on the BSE in the first category.

I have taken into account the 2012 annual reports disclosed by the analysed companies, but also other information available on the companies’ websites and on the Bucharest Stock Exchange website.

Research methodology and hypotheses development.

The first research question will try to find out to what extent Romanian listed companies comply with the disclosure requirements in IFRS.

First of all, I will analyse the information disclosed by each company, as required by IFRS, especially IAS 1. The compliance has been measured through an index, inspired by the IFRS requirements.
Research methodology will be achieved by analyzing the annual reports of companies in the sample, and compliance on a grille made from the reporting requirements of IFRS.

In this study we calculate an index of specific items of disclosure requirements of International Financial Reporting Standard. This index consists of 25 variables.

- Statement of financial position
- Statement of comprehensive income
- Statement of changes in equity
- Cash flow statement
- The existence of compliance with IFRSs declaration and the mention that is the first set of financial statements prepared in accordance with IFRS
- Company information and presentation currency
- Information about the standards and interpretations issued but not yet applied
- Reconciliation between IFRS and principles of previous years
- Presentation and accounting policies Basis of preparation
- Business continuity
- Date the financial statements were authorized for issue and who gave that authorization
- Financial Reporting in Hyperinflationary Economies
- Tangible
- Intangible assets
- Method of determining fair value
- Stocks
- Reconciliation of income tax
- Income
- Borrowing costs
- Employee benefits
- Provisions
- Transactions with related parties
- Earnings per share
- Segmental reporting
- Risk management and sensitivity analysis

Based on variables provided we build the next index: \( I = \Sigma V_i \), where „i” is the number of companies in the sample, and will take values between 1 and 25.

Total index is calculated as the unweighted sum of the marks awarded for each information requirement, since we considered that each element has the same importance to users.

For each data requirement will give a variable, depending on the existence and degree of detail of it, as follows:
- 0 if information is missing;
- 0.5 if the information is presented to a minimum;
- 1 if the information is presented in detail.

Given that the value 0 is recorded when information is missing, and the one where the information is recorded in the financial statements are presented in detail shows that the minimum value that can take the index is 0 and the maximum is 25.

To assess the quality of financial reporting through index values above, we consider the following:
- For values equal with 0: Lack of compliance
- For values between 0 and 10 points: compliance reporting is low;
- For values between 10 and 15 points: compliance reporting is moderate;
- For values between 15 and 25 points: compliance reporting is high.
3.2 Analysis of results

Analysing variables set from the international reference, we calculated the index of disclosure.

As we can see in the table above (Fig. 1. The IFRS compliance level), no company has managed to obtain the maximum score, the closest being the biggest company of the sample, how has accumulated 23.5 points out of 25. It did not submit information about the earnings per share achieved and the rate of Capitalisation of borrowing costs. Other information was detailed, providing users with all necessary information about the work done by the company. At the opposite pole is another company, which received the lowest score, 16 points out of 25 maximum allowed. They omitted the presentation of several information required by International Financial Reporting Standards. The differentiation was made particularly in the information disclosed in the notes.

Then, using a four points Likert scale, I will assess the compliance with the IFRS requirements. The way the level of compliance is assessed is described in Fig. 2. As we can see in the Fig 1. the majority of the companies comply with the IFRS requirements.

<table>
<thead>
<tr>
<th>Values of IFRS Compliance index</th>
<th>Compliance level</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>Lack of compliance</td>
</tr>
<tr>
<td>1–10</td>
<td>Low compliance</td>
</tr>
<tr>
<td>11–15</td>
<td>Medium compliance</td>
</tr>
<tr>
<td>16–25</td>
<td>High compliance</td>
</tr>
</tbody>
</table>

Fig. 2. The IFRS compliance assessment method

Fig. 3. Number of Companies complying with IFRS requirements
As expected, larger companies usually disclose more detailed segment information, sustaining other prior studies (Crawford et al., 2012; Berglof and Pajuste, 2005) which have demonstrated that larger companies are usually much more transparent than other companies.

The result is coherently reported in other studies according to which the biggest company of the sample could be a model for other entities having a high level of transparency and communication.

Only two companies showed no reconciliation between IFRS and principles applicable to previous years. Some companies have failed to provide information about the ability to continue operations. All companies have adopted IAS 29 “Financial reporting in hyper-inflationary economies” but two of them had no information on the amounts actually obtained after the restatement.

Regarding the fair value measurement, there is a serious lack of transparency, not presented enough information regarding the assessment methods and assumptions used. There is no information related quantitative fair value, which would be extremely efficient for potential investors. Only four companies present complete information on how to determine fair value.

Regarding income tax reconciliation, it has not been treated by many companies, which may lead to the decrease of investor confidence in the information provided.

Many times, in accounting policies specify that the company applies the capitalization of borrowing costs but not present quantitative information about the capitalization rate used or the amounts capitalized. Four companies have not provided any information about IAS 23 “Borrowing Costs”.

Risk management and the analyses of sensitivity were presented by most of the companies, a sign that they want to protect their employees, customers and investments. One company does not present all the information, and five other companies no sensitivity analyzes.

We believe that more information was needed in the notes to a much better understanding of the value of certain asset and liability items or own capital, and other issues that have a direct impact on the work performed by the companies concerned. It is very useful for certain aspects to be as detailed as this any user can understand more easily the information presented and take a decision as the correct basis.

As numerous studies have indicated that investors prefer financial statements audited by Big4, we examined the hypothesis that companies audited by Big 4 shows more information comply with international reference. This purpose we have, we created a table in which I presented if the auditor is part of the Big 4 or not. As you can see in the table below, only 7 of the 16 companies analyzed have used the services provided by a company of the Big 4.

<table>
<thead>
<tr>
<th>COMPANY</th>
<th>The auditor is part of Big 4? Yes or No</th>
<th>INDEX</th>
</tr>
</thead>
<tbody>
<tr>
<td>No 1</td>
<td>YES</td>
<td>21</td>
</tr>
<tr>
<td>No 2</td>
<td>NO</td>
<td>19</td>
</tr>
<tr>
<td>No 3</td>
<td>NO</td>
<td>18</td>
</tr>
<tr>
<td>No 4</td>
<td>YES</td>
<td>20,5</td>
</tr>
<tr>
<td>No 5</td>
<td>NO</td>
<td>20</td>
</tr>
<tr>
<td>No 6</td>
<td>NO</td>
<td>22,5</td>
</tr>
<tr>
<td>No 7</td>
<td>NO</td>
<td>16</td>
</tr>
<tr>
<td>No 8</td>
<td>NO</td>
<td>18,5</td>
</tr>
<tr>
<td>No 9</td>
<td>YES</td>
<td>19</td>
</tr>
<tr>
<td>No 10</td>
<td>YES</td>
<td>23,5</td>
</tr>
<tr>
<td>No 11</td>
<td>NO</td>
<td>21</td>
</tr>
<tr>
<td>No 12</td>
<td>NO</td>
<td>19</td>
</tr>
<tr>
<td>No 13</td>
<td>YES</td>
<td>22</td>
</tr>
<tr>
<td>No 14</td>
<td>YES</td>
<td>21</td>
</tr>
<tr>
<td>No 15</td>
<td>NO</td>
<td>22</td>
</tr>
<tr>
<td>No 16</td>
<td>YES</td>
<td>18,5</td>
</tr>
</tbody>
</table>

Fig. 4. Membership auditor in Big 4
Previous studies have shown that the information provided by financial statements audited by Big 4 offers a higher level of trust among users. This can be confirmed for us too, so companies audited by Big 4 are the companies with an index of disclosure of specific elements IFRS higher. Even if at first view it can be seen that there are companies audited from outside of Big 4 with a very high disclosure index (e.g. ELECTROMAGNETICA SA Bucharest with an index of 22.5) overall index of companies audited by Big 4 is 20.78 compared to 19.55 of those not audited by Big 4.

Another aspect that I wanted to analyze was to check if largest companies in terms of total asset value, are those that disclose more information regarding the requirements of International Financial Reporting Standard.

Thus, in Fig. 5. “Index of disclosure based on the total value of assets” we equally divided number of companies, the top eight companies based on the highest values of total assets, and the last 8 companies ranked in depending on the total value of assets.

<table>
<thead>
<tr>
<th>COMPANY</th>
<th>TOTAL ASSETS</th>
<th>Disclosure Index</th>
<th>COMPANY</th>
<th>TOTAL ASSETS</th>
<th>Disclosure Index</th>
</tr>
</thead>
<tbody>
<tr>
<td>OMV PETROM S.A.</td>
<td>37410860000</td>
<td>23.5</td>
<td>IMPACT DEVELOPER &amp; CONTRACTOR S.A.</td>
<td>428751857</td>
<td>16</td>
</tr>
<tr>
<td>S.N.G.N. ROMGAZ S.A.</td>
<td>10404960000</td>
<td>22</td>
<td>ROPHARMA SA BRASOV</td>
<td>359110800</td>
<td>19</td>
</tr>
<tr>
<td>C.N.T.E.E. TRANSELECTRICA</td>
<td>4945037279</td>
<td>20.5</td>
<td>PREFAB SA BUCURESTI</td>
<td>285294642</td>
<td>21</td>
</tr>
<tr>
<td>S.N.T.G.N. TRANSGAZ S.A.</td>
<td>3905823847</td>
<td>21</td>
<td>ELECTROMAGNETICA SA BUCURESTI</td>
<td>284493499</td>
<td>22.5</td>
</tr>
<tr>
<td>ALRO SA</td>
<td>2281298410</td>
<td>21</td>
<td>BIOFARM SA</td>
<td>198510399</td>
<td>18</td>
</tr>
<tr>
<td>OLTCHIM S.A. RM. VALCEA</td>
<td>1928724052</td>
<td>19</td>
<td>TURBOMECANICA S.A.</td>
<td>149008474</td>
<td>18.5</td>
</tr>
<tr>
<td>ANTIBIOTICE SA</td>
<td>514317929</td>
<td>19</td>
<td>CONCEFA SA SIBIU</td>
<td>129476727</td>
<td>20</td>
</tr>
<tr>
<td>OIL TERMINAL S.A.</td>
<td>431100381</td>
<td>18.5</td>
<td>SOCEP S.A.</td>
<td>107695098</td>
<td>22</td>
</tr>
<tr>
<td>The average of disclosure index</td>
<td></td>
<td>20.563</td>
<td></td>
<td></td>
<td>19.625</td>
</tr>
</tbody>
</table>

Fig. 5. Index of disclosure based on the total value of assets

It can be seen from this analysis, that the difference is not very high between the average indicelelui disclosure of large companies to smaller ones, 20.563 to 19.625. This is favorable because it means that most companies want to disclose sufficient information that may be useful to users and therefore this will be reflected in the financial condition of companies.

But the analysis performed can be observed that this hypothesis is validated, large companies disclose more information to smaller companies.

Regarding the companies which disclose information about the statement of financial position, they identify in average 0.875 of information about the statement of financial position. The quite high value of the standard deviation (0.223) shows that there are not great disparities between the companies, regarding the number of companies who present information about this variable. It is possible that some companies are more complex than others, but it may also be possible that companies which identify a few or no information about the statement of financial position at all do not understand the requirements of IAS 1, not being able to correctly identify their information.
<table>
<thead>
<tr>
<th>Variables</th>
<th>Observations</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Average</th>
<th>Standard deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Statement of financial position</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,875</td>
<td>0,223606798</td>
</tr>
<tr>
<td>Statement of comprehensive income</td>
<td>16</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Statement of changes in equity</td>
<td>16</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Cash flow statement</td>
<td>16</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>The existence of compliance with IFRSs declaration and the mention that is the first set of financial statements prepared in accordance with IFRS</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,8125</td>
<td>0,25</td>
</tr>
<tr>
<td>Company information and presentation currency</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,96875</td>
<td>0,125</td>
</tr>
<tr>
<td>Information about the standards and interpretations issued but not yet applied</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,65625</td>
<td>0,396600134</td>
</tr>
<tr>
<td>Reconciliation between IFRS and principles of previous years</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,875</td>
<td>0,341565026</td>
</tr>
<tr>
<td>Presentation and accounting policies and the basis of preparation</td>
<td>16</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Business continuity</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,65625</td>
<td>0,473242362</td>
</tr>
<tr>
<td>Date the financial statements were authorized for issue and who gave that authorization</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,90625</td>
<td>0,271952815</td>
</tr>
<tr>
<td>Financial Reporting in Hyperinflationary Economies</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,90625</td>
<td>0,201556444</td>
</tr>
<tr>
<td>Tangible assets</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,75</td>
<td>0,25819889</td>
</tr>
<tr>
<td>Intangible assets</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,8125</td>
<td>0,25</td>
</tr>
<tr>
<td>Method of determining fair value</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,53125</td>
<td>0,385951206</td>
</tr>
<tr>
<td>Stocks</td>
<td>16</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Reconciliation of income tax</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,71875</td>
<td>0,406970515</td>
</tr>
<tr>
<td>Income</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,90625</td>
<td>0,201556444</td>
</tr>
<tr>
<td>Borrowing costs</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,4375</td>
<td>0,309569594</td>
</tr>
<tr>
<td>Employee benefits</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,65625</td>
<td>0,239356777</td>
</tr>
<tr>
<td>Provisions</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,75</td>
<td>0,25819889</td>
</tr>
<tr>
<td>Transactions with related parties</td>
<td>16</td>
<td>0,5</td>
<td>1</td>
<td>0,75</td>
<td>0,25819889</td>
</tr>
<tr>
<td>Earnings per share</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,71875</td>
<td>0,363719214</td>
</tr>
<tr>
<td>Segmental reporting</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,625</td>
<td>0,387298335</td>
</tr>
<tr>
<td>Risk management and sensitivity analysis</td>
<td>16</td>
<td>0</td>
<td>1</td>
<td>0,78125</td>
<td>0,314576435</td>
</tr>
<tr>
<td>TOTAL</td>
<td>16</td>
<td>16</td>
<td>23,5</td>
<td>20,09375</td>
<td>1,951228246</td>
</tr>
</tbody>
</table>

Fig. 6. Statistical description of the number of variables of IFRS identified by Romanian listed companies

If we look carefully, we can see that the standard deviation for the business continuity is the biggest value (0.473), which means that there are great disparities between the companies, regarding the continuity of the company.

At the opposite the smaller value of standard deviation is 0 for many variables like Statement of comprehensive income, Statement of changes in equity, Cash flow statement, Presentation and accounting policies and the basis of preparation, Date the financial statements were authorized for issue and who gave that authorization.
accounting policies and the Basis of preparation and Stocks, which means that are not significant differences between companies in applying the International Accounting Standards.

As we can see the standard deviation for the total variables is 1.951, that means that per total there are no significant differences between companies in applying the International Financial Reporting Standard.

4. CONCLUSIONS

International Financial Reporting Standards is a universal language that an investor understands and way that it can compare the information provided by listed companies on the BSE with other information from other markets. Implementation of IFRS in Romania was something new for both listed companies and local investors, who need explanations of the transition to IFRS and comparable information. The differences were not great for all listed companies due to accounting harmonization process developed in recent years. We believe this change is beneficial since many companies prepared both a set of financial statements under RAS and one under IFRS, at the request of shareholders or financial institutions-banks, so decreasing costs occasioned.

These financial reports are very useful to users of financial information, which according to the category to which they belong, can take investment decisions in the company concerned, contracts, loans, etc. However to make them be useful, the information presented should be comprehensible, relevant, reliable and comparable with those described above or other companies.

The purpose of this article was to analyze the extent of compliance with the requirements of International Financial Reporting Standard of the entities listed on the Bucharest Stock Exchange (BVB first category) and factors that may influence the degree of disclosure of information. The research conducted showed that the entities have made efforts to present the financial reports comply with stakeholder reporting requirements of International Financial Reporting Standards. So most companies have tried to disclose as much information as provided by international reference.

The main limitations of the research related to the small sample size and the subjectivity of research in determining the variables. For financial statements of 2013 is to achieve a similar study to see if the lack of provision of certain information was first effect of applying standards and a more detailed analysis of the elements published by companies that may influence users' decisions, and thus the situation companies.

ACKNOWLEDGEMENT

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FACTORS INFLUENCING UNDERGRADUATE ACCOUNTING STUDENT SATISFACTION. A SURVEY FROM A ROMANIAN UNIVERSITY

Vasile GORGAN
Bucharest University of Economic Studies
vasile.gorgan@cig.ase.ro

Abstract: Universities begin to increasingly realize that they are involved in a fierce competition for students and they must adopt an entrepreneurial approach in order to better serve their customers/students. Assuming that the success of a university is to a large extent determined by the satisfaction of its graduates, this paper aims to analyze the undergraduate accounting student satisfaction from the Bucharest University of Economic Studies. An online questionnaire was used to collect data from students who graduated in 2012 and 2013. The following factors influencing the overall satisfaction were taken into account: self-confidence development, the curriculum, the quality of teaching, extra-curricular activities and career development opportunities, information technology facilities and colleagues’ quality. An analysis of the most important factor in determining the overall satisfaction was performed. Limitations of the study and future research directions are also presented.

Keywords: customer satisfaction, higher education, teaching quality

1. INTRODUCTION

In the context of globalization, competition is present everywhere and higher education system is not an exception. In recent years, under the impact of social needs development and labor market transformations, universities have begun to increasingly realize that they are involved in a fierce competition for students and they must adopt an entrepreneurial approach in order to better serve their customers/students (Petruzzellis, D’Uggento, & Romanazzi, 2006). A paradigm shift occurred in the higher education system where market-type mechanism have been introduced even in countries previously characterized by a high degree of government control, marketisation being seen as a compromise between privatization, academic autonomy and state control (Hemsley-Brown, 2006).

Romanian universities are part of this trend of increased competition. The transformation they underwent has begun after political and economic reforms that followed the fall of communism in 1989. On the background of high school graduates normal desire to obtain a higher education diploma, the number of universities increased from 46 in November 1989 to 126 in 2000, and the number of students enrolled from 215,226 to 907,353 in 2007/2008 (Filip, 2012). These increase was supported on one hand by the emergence of private universities which tried to achieve greater market share and on the other hand by the increased number of students enrolled by public universities as the number of students was the main proxy for their revenues. The demand was driven by the freshly high school graduates and also by older people who, due to relaxation of admission conditions compared to previous period, have now access to higher education. In the last years the demand from the latter decreased dramatically so that now it is determined almost exclusively by the number of freshly high school graduates. In addition, demographic trends showing important decrease after 90’s leaved their marks on demand for higher education programs. These are the reason why, in the last years, many Romanian universities are facing difficulties in attracting enough students in order to assure at least the survival of academic
programs. Under these circumstances the adoption of measures intended to increase the quality of services offered to students is a must.

In relation to education in accounting it must be noted that after the fall of communism in 1989, in Romania a series of economic reforms were initiated in order to incorporate western business principles. These reforms dramatically influenced all economic fields and consequently the accounting system. The first reform of accounting system occur in 1994 when Romania started to apply an accounting model of French inspiration. In 1999 the process of accounting harmonization of the national accounting system of large entities with the 4th EU Directive and IASs was started. This process continued in 2005 when another ministerial order was issued, with the purpose to prepare for Romania’s accession to EU. Full enactment of the 4th and 7th EU Directives was pursuit and the order was applicable to all entities. As of 2010 a modified version was issued. International Financial Reporting Standards are mandatory for listed companies in consolidated accounts and financial institutions as of January 1, 2007 (Albu, Albu, & Alexander, 2013). All these changes add significant strains to accounting education, teachers and students together having to face these changes.

2. LITERATURE REVIEW

Fariba & Masomeh (2011) believe that development of higher education quality is a very important aspect which is part of management and marketing of any university in the world (Munthiu, Turțoi, Tuță & Zara, 2014). Quality of education is necessary condition of university’s competitiveness in context of international integration and high domestic competition. (Kalenskaya, Gafurov & Novenkova, 2013). Quality in this field is a complex, multifaceted and quite relative concept given the existence of various stakeholders (students, parents, staff, employers, business and legislators, government, professional bodies etc.) with their own view of quality based on their particular needs (Petruzzellis, D’Uggento & Romanazzi, 2006) (Gruber, Fuß, Voss & Glaeser-Zikuda, 2010). Starting from the premise that students are the “primary customers” of a university, student-perceived service quality is considered an extremely important issue for universities and their management (Brochado, 2009) (Gruber, Fuß, Voss & Glaeser-Zikuda, 2010). Assessing student satisfaction creates premises for universities to attract and retain those students that best matches institution’s capabilities and to create competences that will better serve the various needs of student populations (Letcher & Neves, 2010). On the other hand universities invest enormous efforts to lift their position in various ranking systems that, to some extent, include some measure of student satisfaction.

According to Giese and Cote (2000) although there are a lot of various definitions for customer satisfaction, they tend have in common three elements: 1) consumer satisfaction is an emotional or cognitive response; 2) the response pertains to expectations, product, consumption experience, etc.; and 3) the response occurs at a particular time (after consumption, after choice, based on accumulated experience, etc.).

Student satisfaction is a highly debated topic in the literature with quite diverse views of the authors on the concept. Elliot and Shin (2002) define student satisfaction as “the favourability of a student’s subjective evaluation of the various outcomes and experiences associated with education” (Elliott & Shin, 2002). According to Wiers-Jenssen (2002) student satisfaction is an interesting concept because the factors perceived to be of most importance differ between institutions and subject fields because of variations in the study programs offered, location, size and complexity of the institutions. This might be the reason why there are a lot of articles attempting to clarify the concept, develop measures to quantify it and to identify the factors that influences its level.

Previous study on student satisfaction targeted, among others, satisfaction with various learning systems (e-learning, blended e-learning, distance education, team learning, etc.), factors that influences the overall satisfaction, proposal of new measurement tools for student satisfaction. These studies uses specific models and instruments developed by their authors, the results not being
easily comparable. The following paragraph briefly reviews the main results of studies on student satisfaction.

Letcher & Neves (2010) conducted a study on students of a business program from United States whose results revealed that among the factors that influence the overall satisfaction, self-confidence, extra-curricular activities and career opportunities, and quality of teaching in general are the factors with greater impact on satisfaction. Another study on student satisfaction in a blended e-learning system environment found that computer self-efficacy, performance expectations, system functionality, content feature, interaction, and learning climate are the primary determinants of student learning satisfaction with such a system (blended e-learning system environment) (Wu, Tennyson & Hsia, 2010). The results of a study pertaining to Italian universities showed that satisfaction seems to be mainly influenced by economic conditions and by a positive but narrow attitude that leads students to appreciate universities in the region of origin (Petruzzeellis, D’Uggento & Romanazzi, 2006). The study conducted by Farrel & Farrel (2008) on cooperative learning used into International Accounting, revealed that cooperative learning “created supportive team experiences that assisted them to develop discussion skills and better engage with the content of International Accounting”. Opdecam & Everaert (2012) deem that higher level of satisfaction and a more positive course experience are reported by students that are involved in team learning condition compared to students in a traditional lecture-based control condition.

The current study uses Letcher & Neves’ approach, aiming to identify the overall satisfaction and factors that have the highest impact on this level.

3. RESEARCH METHODOLOGY

This study used questionnaire as an instrument to obtain the data needed. The questionnaire was adapted after “EBI’s Undergraduate Business Exit Assessment” which is an instrument developed by Educational Benchmarking, Inc. and is designed for business undergraduate programs. The decision to use this instrument was determined by fact that it is a quite popular survey in United States, used in about 150 business schools and collecting data from around 30000 students annually (Letcher & Neves, 2010). The survey underwent a series of transformations in order to adapt it to particularities of Faculty of Accounting from the Bucharest University of Economic Studies. The modified questionnaire included 7 demographic variables and 40 Likert type questions with the scale interval of 7 (Extremely dissatisfied to Extremely satisfied with no verbal labels for scale points 2 through 6) that are concerned with overall satisfaction and satisfaction with each of the following factors: a) self-confidence of graduates (Factor 1), b) curriculum, instruction and classes (Factor 2), c) technology facilities (Factor 3), d) colleagues’ quality (Factor 4), e) quality of teaching of the major areas in the curriculum (Factor 5), extra-curricular activities and career development opportunities (Factor 6). The main changes relative to original questionnaire concerned questions related to Factor 5, as the Faculty of Accounting curriculum is quite different from that of business program, to questions that pertains to satisfaction with major courses/required courses as this distinction is not quite popular in Romanian higher education system. Also the questions related to student advising were not included in our survey as this type of activities are almost nonexistent in Romanian universities.

A number of 685 emails were sent to graduates of Faculty of Accounting and Management Information Systems, Class of 2012 and 2013. They were asked to fill the online questionnaire. A number of 59 responses were received which provided a response rate of 8.61%.

The first factor tested for its influence on overall satisfaction is called **self-confidence (Factor 1)** and it includes items that tries to capture the perception of one’s own abilities, which seems to be a proxy for self-esteem. These items relates to satisfaction on: presentation skills in native language (Romanian), presentation skills in a language of international circulation, ability to work in team, ability to use a manage information technologies, critically thinking, ability to define and solve problems, ability to analyze and interpret data.
The second factor (Factor 2) tries to capture the satisfaction with curriculum, instruction and classes and the items involved are: quality of teaching in Accounting, satisfaction with the correlation between Grades and the perceived level of student’s performance, accessibility of instructors outside of class, instructor’s responsiveness to student concerns, instructors’ ability to present concepts from real world, to present a global perspective, social responsibility, technology and ethical issues, satisfaction with value derived from team experiences and satisfaction with the size of courses. Technology facilities (Factor 3) is assessed through items that pertain to: computers availability, satisfaction with remote access to university network and training to utilize computing resources. Colleagues’ quality (Factor 4) includes items that pertain to academic quality of fellow students, ability to work in teams and level of camaraderie. Quality of teaching of the major business areas in the curriculum (Factor 5) capture the level of satisfaction with the following courses: Accounting, Audit, Information Systems, Economics, Business Law, Financial and economic analysis. The factor named extra-curricular activities and career development opportunities (Factor 6) relates to opportunities for practical experiences and interaction with practitioners, the activities of student organizations, university support in searching for a permanent job, access to student organizations in order to cultivate career opportunities and the number of companies participating in campus recruiting programs and the quality of these companies. The overall satisfaction was captured through questions that pertain to global fulfillment of expectations related to undergraduate accounting program, the perceived value of the program and willingness to recommend the accounting program to a close friend. An average score was computed for each factor and for overall satisfaction for every respondent.

4. RESULTS AND DISCUSSION

Data gathered through the online survey was processed using Microsoft Excel and IBM SPSS Statistics. Results show a mean value for overall satisfaction level of 4.78 on a scale from 1 to 7 which means that, on the average, the graduates of the accounting program are somewhat satisfied. The factor that scored best was Factor 5-Quality of teaching of the major business areas in the curriculum. We think this is a positive result especially in the context of changes undergone by the Romanian Accounting system in the last 25 years. The lowest score was 3.54 and was obtain for Factor 6- extra-curricular activities and career development opportunities. We believe this low score is due to drawbacks of higher education system during the Communist Era, where such activities were almost nonexistent because every student used to obtain a job after graduation on the basis of overall mark received during the undergraduate program, and somehow this situation does not seem to have changed much since then.

<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Factor 1</td>
<td>59</td>
<td>2,00</td>
<td>7,00</td>
<td>4,6154</td>
<td>1,21295</td>
</tr>
<tr>
<td>Factor 2</td>
<td>59</td>
<td>1,00</td>
<td>7,00</td>
<td>4,5102</td>
<td>1,38473</td>
</tr>
<tr>
<td>Factor 3</td>
<td>59</td>
<td>1,00</td>
<td>7,00</td>
<td>4,2203</td>
<td>1,59501</td>
</tr>
<tr>
<td>Factor 4</td>
<td>59</td>
<td>1,00</td>
<td>7,00</td>
<td>4,7798</td>
<td>1,37910</td>
</tr>
<tr>
<td>Factor 5</td>
<td>59</td>
<td>1,60</td>
<td>7,00</td>
<td>5,0780</td>
<td>1,24348</td>
</tr>
<tr>
<td>Factor 6</td>
<td>59</td>
<td>1,00</td>
<td>7,00</td>
<td>3,5405</td>
<td>1,45678</td>
</tr>
<tr>
<td>OverallSatisfaction</td>
<td>59</td>
<td>1,00</td>
<td>7,00</td>
<td>4,7851</td>
<td>1,46190</td>
</tr>
<tr>
<td>Valid N (listwise)</td>
<td>59</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Fig. 1. Descriptive statistics for factors influencing the overall satisfaction of accounting program graduates
Further, a stepwise regression was performed in SPSS. The initial model included six factors. After the regression analysis only two of them were retain as explanatory variables for overall satisfaction: **Factor 1- self-confidence** and **Factor 6- extra-curricular activities and career development opportunities**. Both of them are positively correlated with the overall satisfaction (the value of Pearson coefficient $r=0.747$ with $p<0.001$ for Factor 1 and $r=0.677$ with $p<0.01$ for Factor 6) and the model which includes them accounts for 61.6% of the variance (the adjusted R Square is .616).

![Fig. 2 Model summary](image)

Although Factor 2, Factor 3 and Factor 5 are also positively correlated with the overall satisfaction as can be seen in the table below, their inclusion does not increase the explanatory power of the model.

![Fig. 3 Correlation matrix](image)

### 5. CONCLUSION AND RESEARCH LIMITATIONS

A paradigm shift occurred in the higher education system where market-type mechanism have been introduced even in countries previously characterized by a high degree of government control. Universities have begun to increasingly realize that they are involved in a fierce competition for students and they must adopt an entrepreneurial approach in order to better serve their customers/students. Under these circumstances a study was conducted at the Faculty of Accounting and Management Information Systems from the Bucharest University of Economic Studies, trying to identify the overall satisfaction of graduates and the factors that influences its level. The following factors influencing the overall satisfaction were taken into account: self-confidence development, the curriculum, the quality of teaching, extra-curricular activities and career development opportunities, information technology facilities and colleagues’ quality. The results of
the study showed that the accounting program is somewhat satisfying for its graduates. The study also revealed that only two factors are enough to predict the overall satisfaction: self-confidence (Factor 1) and extra-curricular activities and career development opportunities (Factor 6). Limitation of the study resides in the limited context of respondents who come from only one faculty and only two graduation years and therefore generalized conclusions cannot be drawn. Future research will target an increased number of respondents from more universities and more graduation years.

ACKNOWLEDGEMENT
This work was cofinanced from the European Social Fund through Sectoral Operational Programme Human Resources Development 2007–2013, project number POSDRU 159/1.5/S/142115 “Performance and excellence in doctoral and postdoctoral research in Romanian economics science domain”.

BIBLIOGRAPHY


MANAGEMENT ACCOUNTING TOOLS: SUPPORT FOR INTEGRATED REPORTING

Gabriel JINGA
Bucharest University of Economic Studies
Gabriel.Jinga@cig.ase.ro

Mădălina DUMITRU
Bucharest University of Economic Studies
madidumitru2007@gmail.com

Abstract: Sustainability concerns characterize the times we live. Big companies have to deal with sustainability in order to legitimize themselves in front of their stakeholders. A new form of reporting, the integrated reporting, is emerging and many international bodies (International Integrated Reporting Council – IIRC, Global Reporting Initiative, Sustainability Accounting Standards Board etc.) are publishing guidelines which include what does a company has to publish in a report. We argue that many key performance indicators included in a(n integrated) report are produced by management accounting. We consider that in the companies’ path to sustainability the management accounting will play an important role. As such, in this paper, we present an analysis of the management accounting tools used in preparing integrated reports. Our research relies on the reports published on their websites by two companies included in the IIRC’s Pilot Program: Novo Nordisk and Takeda.

Keywords: management accounting tools, integrated reporting, annual reports, IIRC

1. INTRODUCTION

Management accounting is seen as the producer of accounting information, especially for internal purposes. During the last decades, the business world has changed considerably, along with the globalization, the economic crisis etc. One challenge that lies ahead of the modern companies is the sustainability.

Many bodies were involved in the sustainability reporting in the last period. Among them, the International Integrated Reporting Council (IIRC) was formed in 2010 with the declared purpose to prepare the first international integrated reporting framework. In its work, the IIRC was supported by a group of companies which joined its Pilot Program. In this article, we analysed the reports published by two of these companies, in one domain (Pharmaceutical and Biotechnology): Novo Nordisk and Takeda.

Also companies may consider sustainability reporting for external stakeholders, in order to be seen by them as behaving in a sustainable way, it can be used for the internal management, too, to improve the processes. Many companies report an improved economic performance after integrating sustainability in their decision-making. From the point of view of the integrated reporting, this transformation of the processes used within the company is embedded into the integrated thinking.

Management accounting can provide a set of tools that can help pilot a company whose management is interested in the sustainability issues. Top management’s priorities are to secure the survival of the company by assuring its profitability and by obtaining resources from its key stakeholders. In order to achieve its goals, top management needs highly aggregated financial and strategic information about the business environment and the performance of the company (Burritt, Hahn and Schaltegger, 2002). Our research question is which are the tools provided by the (environmental) management accounting helping the companies in preparing the integrated reports.
The rest of this paper will continue as follows: first, we will present a theoretical background supporting our work; next, we will describe the research methodology used in this article; the following section is dedicated to the results of our study; the paper ends with the discussion and conclusions of our work.

2. LITERATURE REVIEW

Doing business in a sustainable way generates changes within all the areas of the company. This includes the management accounting. Its tools are used by the modern organizations to measure, define, and report internally and externally the economic, social and environmental impact of the company.

Previous studies (Bouten and Hoozee, 2013) present the following environmental management accounting (EMA) tools used by the companies: capital investment decision making, budgeting, performance measurement, incentive system, costing. Other authors (Burritt et al., 2002) classify the EMA tools into monetary environmental management accounting (MEMA) and physical environmental management accounting (PEMA). The tools are past- or future-oriented, short- or long-term, ad-hoc or routinely generated. These tools are: environmental cost accounting; environmentally-induced capital expenditure and revenue; ex-post assessment of relevant environmental costing decisions; ex-post inventory assessment of projects (including life cycle costing – LCC); monetary environmental budgeting; environmental long-term financial planning; relevant environmental costing; monetary environmental investment appraisal; material and energy flow accounting; environmental capital impact accounting; ex-post assessment of short-term environmental impacts; ex-post inventory appraisal of physical environmental investments (including life cycle assessment – LCA); physical environmental budgeting; environmental long-term physical planning; tools designed to predict relevant environmental impacts; physical environmental investment appraisal.

The response of the company to sustainability pressures depends on its specific context, determined by the environmental disturbances, top management commitment, operational leadership and internal power relations (Larrinaga-González and Bebbington, 2001; Fraser, 2012; Gorgan, Dumitru and Gorgan, 2014).

Previous studies show a relationship between the development of EMA tools and the environmental disclosures in the annual reports (Frost and Seamer, 2002). There are companies which first develop a set of key performance indicators and then publish the results in the annual reports (e.g. Bartolomeo, 1998, cited by Bouten and Houzee, 2013). In other companies happens the opposite: the reporting drives the conception of a more representative set of indicators (Bennett and James, 1998; Adams and Frost, 2008). Other studies (Bouten and Houzee, 2013; Duncan and Thomson, 1998) reveal that the environmental reporting and EMA depend on a number of factors: the strength of the environmental disturbances, top management commitment and the presence of an environmental champion. Laughlin (1991, cited by Contrafatto and Burns, 2013), mentions three “environmental jolts”:

1. increased regulation;
2. a general increase at societal level of the importance of such issues as climate change and human rights’ protection, and
3. other expected legislation which management aims to anticipate.

King and Roberts (2013) indicate five forces making the company invest in sustainability: investors, big customers, increasing regulation, social pressures, reduce wastage of resources.

Nowadays, there are many bodies in the world which want to establish key performance to be disclosed by the companies. For instance, the most used guidelines in the sustainability reporting are the ones published by the Global Reporting Initiative, who recently published its fourth generation of standards. Also, in Europe the European Federation of Financial Analyst Societies and DVFA publish guidelines including indicators to be disclosed by companies grouped on
activity domains. In USA, in 2012 the Sustainability Accounting Standards Board was formed. It’s “mission is to develop and disseminate sustainability accounting standards that help publicly-listed corporations disclose material factors in compliance with SEC requirements” (sasb.org). IIRC considers that prescribing a set of key performance indicators (KPIs) and measurement methods is beyond the scope of a principle-based framework. Yet, it considers “a project to develop a database of authoritative, external sources of KPIs” (IIRC, 2013).

There is evidence that KPIs are becoming more formally constituted in strategic planning and control and that the information provided by management accounting “is required to be holistic, integrated, and predictive as well as historical” (Contrafatto and Burns, 2013).

Sustainability will change the way managers think about their companies. According to King and Roberts (2013), the company’s strategy, risks, opportunities and financial performance and the impacts it has on society and the environment are inseparable. This requires setting an integrated strategy. Integrated thinking can encompass innovation, such as efficiencies in business processes, products and inputs.

3. RESEARCH METHODOLOGY

Our research relies on the longitudinal analysis of the reports published by the companies belonging to one activity domain, included in the IIRC Pilot Program Business Network, namely: Novo Nordisk and Takeda, in the Pharmaceuticals and Biotechnology domain. We selected the Pharmaceutical and Biotechnology domain because the company that publishes the most rewarded integrated reports, Novo Nordisk (NN), activates in this domain.

We analysed all the reports published on the companies’ websites. Thus, we analysed the following reports:

<table>
<thead>
<tr>
<th>Company/Years</th>
<th>Report</th>
</tr>
</thead>
<tbody>
<tr>
<td>NN</td>
<td>1995 Environmental Report</td>
</tr>
<tr>
<td></td>
<td>1996 Environmental Report and Social Report</td>
</tr>
<tr>
<td></td>
<td>1997 Environmental Report</td>
</tr>
<tr>
<td></td>
<td>1998 Environmental Report and Social Report</td>
</tr>
<tr>
<td></td>
<td>1999–2000 Environmental and Social Report</td>
</tr>
<tr>
<td></td>
<td>2001 Triple Bottom Line Report</td>
</tr>
<tr>
<td></td>
<td>2002–2003 Sustainability Report</td>
</tr>
<tr>
<td></td>
<td>2004–2013 Integrated Report</td>
</tr>
<tr>
<td></td>
<td>2009–2013 Integrated Report and CSR Data Book</td>
</tr>
</tbody>
</table>

Source: compilation of the authors

We grouped the research results on companies.

In terms of evidence of using the management accounting tools, we searched for the following items: investment decisions, budgets, costs, performance measurement (through ad-hoc; parallel, strategic or integrated indicators), incentives systems, balanced scorecard, life-cycle analysis. All the items were searched related to environmental and social aspects. We searched for quantitative indicators, as we consider that these can be generated by the management accounting.

4. RESEARCH RESULTS

After analysing the reports published by the companies, we found evidence of using the following management accounting tools:
Tab. 2. Management accounting tools used by the company, according to their annual reports

<table>
<thead>
<tr>
<th>Company</th>
<th>Investment decisions</th>
<th>Budgets</th>
<th>Costs</th>
<th>Performance measurement</th>
<th>Incentives systems</th>
<th>Balanced scorecard</th>
<th>Life-cycle</th>
</tr>
</thead>
<tbody>
<tr>
<td>NN</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Takeda</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>

Source: compilation of the authors

We further detail the profile of the company, their evolution in terms of sustainability and the specific evidence regarding the (environmental) management accounting that we encountered.

a) NN

NN was established in 1923 in Denmark. It is the leader in the diabetes medicines. It also produces medicines for obesity, haemophilia, growth disorders or inflammation. Its corporate philosophy is the Novo Nordisk Way. It includes “balancing financial, social and environmental considerations”. NN was one of the first companies in the world to publish an integrated report (in 2004).

In 2013 the company had more than 24.3 million patients using diabetes products, 38,436 employees, 125 thousand tons CO₂ emissions and 2,685 thousand m³ water consumption.

The evolution of the sustainability jolts in NN’s environment and the company’s response is presented in the following table:

Tab. 3. Sustainability jolts and reporting practices at NN

<table>
<thead>
<tr>
<th>Year</th>
<th>Sustainability jolts</th>
<th>Reporting evolution</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990–2000</td>
<td>New Danish green accounting regulations</td>
<td>Publication of individual site reports for the major production plants to address local stakeholders needs</td>
</tr>
<tr>
<td></td>
<td>Verifier’s recommendation</td>
<td>• Continuation of the LCA (life-cycle) program</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Further discussion of global operating standards and biosafety issues in relation to operations and products</td>
</tr>
<tr>
<td></td>
<td>Signatory of International Chamber of Commerce’s Business Charter for Sustainable Development in 1991</td>
<td>Establishment of Corporate Environmental Board</td>
</tr>
<tr>
<td></td>
<td>Track progress and generate the necessary data for the Environmental Report</td>
<td>Establishment of a formal management system</td>
</tr>
<tr>
<td>Legislation worldwide</td>
<td></td>
<td>Set regulatory limits for each type of emissions</td>
</tr>
<tr>
<td></td>
<td>• NN’s tradition and Environmental Policy</td>
<td>• Dialogue with environmental stakeholders</td>
</tr>
<tr>
<td></td>
<td>• Raw materials impact</td>
<td>• Press conferences</td>
</tr>
<tr>
<td></td>
<td>• Products assessment</td>
<td>• Web page since 1996</td>
</tr>
<tr>
<td></td>
<td>• Facilities and operations</td>
<td>• Position papers</td>
</tr>
<tr>
<td></td>
<td>• Dow Jones Sustainability Group Index</td>
<td>• Environmental sponsorships</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Environmental training</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• More focus on suppliers</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Enzyme Business Packaging Policy</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• “Values in Action” project</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Life-cycle analyses</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Waste management and new targets</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Energy efficiency agreement with the Danish Energy Agency</td>
</tr>
<tr>
<td>Member of GRI</td>
<td></td>
<td>Member of GRI</td>
</tr>
<tr>
<td>Target: to define a model for stakeholder dialogue and involvement</td>
<td>Application of the guidelines in the report</td>
<td></td>
</tr>
<tr>
<td>Member of World Business Council for Sustainable Development</td>
<td>Stakeholder workshop – first dialogue with stakeholders in this field</td>
<td></td>
</tr>
</tbody>
</table>

International project to develop internationally standardised eco-efficiency indices.
NN acknowledges the need for integrated reporting since 1996, the year when it starts including financial information on the environmental performance.

Regarding investment decisions, NN discloses investments regarding the odour, noise, a purification plant, a waste recycling and treatment centre, a wastewater plant etc. It also discloses the amounts of the investments.

In terms of budgets, until 2000 it only presents some plans, without figures. The plans are made for the next year. In 1998, it declares setting local targets, at least for water and energy eco-productivity. In 1999, the targets refer to: sustainable development, overall social responsibility, employees, health and safety, human rights, suppliers, environmental management, environmental performance, bioethics. In the last reports the environmental targets are set for: energy consumption, water consumption, CO\textsubscript{2} emissions from energy consumption. For the social part, three targets are set, as well: patients reached with Novo Nordisk diabetes care products in millions, working the Novo Nordisk Way, diverse senior management teams.

The environmental costs include:

<table>
<thead>
<tr>
<th>Year</th>
<th>Estimated costs for waste management</th>
<th>Handling and disposal of solid waste</th>
<th>Environment costs (not refundable)</th>
<th>Energy, SO\textsubscript{2} and CO\textsubscript{2} taxes (non-refundable)</th>
<th>Running of environmental departments in Denmark</th>
<th>Running of environmental departments</th>
<th>Remediation cost for polluted sites</th>
<th>Remediation cost for polluted sites</th>
<th>Biomass management (including transportation, treatment and capacity costs of running the department)</th>
<th>Biomass management (including transportation, treatment and capacity costs of running the department)</th>
<th>Net cost of wastewater treatment at municipal plants</th>
<th>Net cost of wastewater treatment at municipal plants</th>
</tr>
</thead>
<tbody>
<tr>
<td>1996</td>
<td>Costs incurred to manage environmental impacts of the operations</td>
<td>Remediation cost for polluted sites</td>
<td>Other activities relating to their environmental strategy, as well as and their aim to be an environmentally responsible corporate citizen</td>
<td>Remediation cost for polluted sites</td>
<td>Biomass management (including transportation, treatment and capacity costs of running the department)</td>
<td>Biomass management (including transportation, treatment and capacity costs of running the department)</td>
<td>Net cost of wastewater treatment at municipal plants</td>
<td>Net cost of wastewater treatment at municipal plants</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1997</td>
<td>Handling and disposal of solid waste</td>
<td>Energy, SO\textsubscript{2} and CO\textsubscript{2} taxes (non-refundable)</td>
<td>Running of environmental departments</td>
<td>Running of environmental departments</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1999</td>
<td>Handling and disposal of solid waste</td>
<td>Environmental taxes (not refundable)</td>
<td>Costs incurred to manage environmental impacts of the operations</td>
<td>Remediation cost for polluted sites</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2000</td>
<td>Running of environmental departments</td>
<td>Remediation cost for polluted sites</td>
<td>Other activities relating to their environmental strategy, as well as and their aim to be an environmentally responsible corporate citizen</td>
<td>Remediation cost for polluted sites</td>
<td>Biomass management (including transportation, treatment and capacity costs of running the department)</td>
<td>Biomass management (including transportation, treatment and capacity costs of running the department)</td>
<td>Net cost of wastewater treatment at municipal plants</td>
<td>Net cost of wastewater treatment at municipal plants</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: compilation of the authors
It includes environmental and social indicators for performance measurement since 1995. In 1993 they were already computing an “integrated” indicator, namely Eco-productivity index (EPI). This is computed as indexed turnover in constant prices/indexed resource consumption *100. EPI is computed for water, energy and raw materials. In 1998, the company starts computing EPI for basic production at “a site and divisional level and can thereby be used in the internal management decision-making process”. The site-based EPI is production (1998)/production (1997) *water or energy consumption (1998)/water or energy consumption (1997) *100. In 2006, EPI is replaced by Eco Intensity Ratios (EIR). EIR is defined as “resource consumption per produced or released unit”.

Important decisions regarding the reported non-financial KPIs are made in 2009. Thus, on one hand, six new KPIs are published “to reflect current priorities and enhance transparency” (diverse senior management teams, managers trained in business ethics, people participating in clinical trials, volume of wastewater, non-hazardous waste, CO₂ emissions from cooling agents). On the other hand, twelve KPIs are not disclosed anymore (for instance, EIR). The decision is explained by the fact that those KPIs “are not used to drive performance, and hence do not qualify for inclusion as performance indicators”. Another set of five KPIs was included only in the notes (for instance, fatalities due to occupational injuries).

There is evidence that the company is using life-cycle assessment and balanced scorecard. Since 1995, they started working on a management system including sustainability issues.

NN was one of the first companies to disclose information about environmental accounting and social accounting, which are defined as parts of the financial accounting. Thus, in 1998, the environmental statement reflects: “corresponding costs, investments, and income that form part of our annual reports for 1998 and 1997. They comprise selected traceable costs which include end-of-pipe pollution abatement measures, energy taxes and running costs for the environmental departments”.

In 2014 social performance is directed in three areas: patients, employees and assurance that NN is a responsible business.

b) Takeda

Takeda is the leading pharmaceutical company in Asia (“a world-class pharmaceutical company with Japanese origin” which “contributes to the health of individuals worldwide”), whose history dates back to the year 1781. The company sold traditional Japanese and Chinese medicines in the beginning. In 1895, Takeda established its first pharmaceutical factory in Osaka, producing analgesics. After World War II the company was engaged in manufacturing vaccines. In 1940 the company formulated Nori: “making contributions to society is the most basic and important thing for corporate management having the public nature of business in mind”. In 1960 it enters the global market, by establishing a manufacturing and marketing company in Taiwan. The European market (1978) and the United States (1980s) followed. Their core therapeutic areas are: Cardiovascular & Metabolic; Oncology; Central nervous system (CNS) diseases; Respiratory & Immunology; General medicine (gastrointestinal & genitourinary); Vaccine (Annual Report, 2012).

Its corporate philosophy is the Takeda-ism, meaning “producing medicine through integrity (fairness, honesty and perseverance)”. As a pharmaceutical company, the R&D is a core subject at Takeda. The R&D principles are: urgency; innovation; measurement; partnership.

The company sees the social action programs as “investment in society”, considering them one of the important company activities. “The concept is deeply entwined in our genes”. The landmarks in their sustainability activities and the sustainability jolts leading to them can be summarized as follows:
Tab. 5. Sustainability jolts and reporting practices at Takeda

<table>
<thead>
<tr>
<th>Year</th>
<th>Sustainability jolts</th>
<th>Reporting evolution</th>
</tr>
</thead>
<tbody>
<tr>
<td>1963</td>
<td>Society concern of social issues</td>
<td>Establishment of the Takeda Science Foundation</td>
</tr>
<tr>
<td>1974</td>
<td>Society concern of environmental issues</td>
<td>Energy Conservation Committee was established</td>
</tr>
<tr>
<td>1990–2000</td>
<td>• Launch of the Japan Responsible Care Council</td>
<td>• Takeda starts to implement responsible care activities</td>
</tr>
<tr>
<td></td>
<td>• Employees’ human rights</td>
<td>• Enacted “Takeda Code of Compliance Standards”</td>
</tr>
<tr>
<td></td>
<td>• Launch of the Japan Responsible Care Council</td>
<td>• Formulated “Basic Principles on the Environment”</td>
</tr>
<tr>
<td></td>
<td>• Employees’ human rights</td>
<td>• Promotes waste reduction since 1993</td>
</tr>
<tr>
<td>2000–present</td>
<td>• “To facilitate understanding of Takeda’s activities in a comprehensive manner, through the provision of both financial and non-financial information, including CSR activities”</td>
<td>• Publication of integrated reports</td>
</tr>
<tr>
<td></td>
<td>• Increasing recognition of “corporate social responsibilities”</td>
<td>• Launches the “Basic Policy on Social Contribution” and the CSR Promotion Committee led by the President.</td>
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<td></td>
<td>• Participation in the UNGC (LEAD) Program</td>
<td>• Formulated the Global Code of Conduct</td>
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<td></td>
<td>• Inclusion in SRI (Dow Jones Sustainability Asia Pacific Index, FTSE4Good etc.)</td>
<td>• Launched Takeda Initiative</td>
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<td>• Inclusion in the IIRC’s Pilot Program</td>
<td>• In 2006 launched Takeda Women’s Network</td>
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<td>• Inclusion in the IIRC’s Pilot Program</td>
<td>• Launched Takeda Total Human Safety net (THS)</td>
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<tr>
<td></td>
<td>• Inclusion in the IIRC’s Pilot Program</td>
<td>• Uses the GRI G4, UNGC Advanced Level Criteria, ISO, AA1000</td>
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</table>

Source: compilation of the authors

Takeda is considering the environment in investment decisions. For instance, it declares purchasing hybrid cars for commercial use within the Tokyo metropolitan area since March 2008.

Regarding the budgets, they set targets until fiscal 2017.

Regarding the environmental reporting, it includes in the Highlights: total input energies, CO₂ emissions, fresh water used. As social reporting indicators, it includes in the Highlights the number of employees. In terms of quantitative indicators included in the section dedicated to the Environment in the last annual report it includes seven indicators: amount of water used and discharged of the group, CO₂ emissions of the group, SO₂ (sulfur oxide) emissions, NOₓ (nitrogen oxide) emissions, dust emissions, amount of waste generated, PRTR-designated substances released into the atmosphere (Japan). In the section dedicated to Labor in the last integrated report, the company is only presenting the women’s empowerment initiatives in figures. Also, regarding the Corporate Citizenship Activities, four quantitative indicators are presented: number of participants in the global leadership development program, Takeda Science Foundation research grants, Shoshisha Foundation scholarships, Institute for Fermentation, Osaka, research grants.

The company declares offering incentives to employees involved in volunteering activities, in the form of days off.

In 2007 it describes the environmental protection costs and it declares using environmental management accounting in the first reports. The environmental protection costs include business area costs (pollution prevention costs, global environmental protection costs, resource circulation costs), upstream/downstream costs, administration costs. They are presented in terms of investment and expenditure. The company has a strategy of enhancing the R&D pipeline through product life-cycle management.
The sustainability is included in its strategy, as in 2013 it states that the “plans include assessment and analysis of the environmental impact of Group products over their life cycle and a detailed approach to environmental accounting through utilization of LIME\(^1\) and other means”.

5. DISCUSSION AND CONCLUSIONS

We selected these two companies for presentation in our article as they are activating in the same domain (Pharmaceuticals and Biotechnology), thus making the comparison easier. In the same time, we notice that their history in integrated reporting is longer than that of the international bodies involved in this new form of reporting (NN prepares the first integrated report for 2004, Takeda prepares it for 2006, the IIRC is formed in 2010).

One of the contributions of our article is that we performed an analysis of integrated reports, including economic, social and environmental data. Previous articles were directed in general to one form of reporting, for instance environmental reports.

Our research question was to identify the (environmental) management accounting tools supporting the companies when preparing the integrated reports. The first step was to prepare a list of tools encountered in previous research articles. Thus, we identified: investment decisions, budgets, costs, performance measurement, incentives systems. When analysing the reports published by the two companies, we added to our list: balanced scorecard, social accounting, environmental accounting, management systems, life-cycle accounting. The two companies are using the same number of tools, with NN not declaring using incentives systems and Takeda not declaring using balanced scorecard.

We notice that the environmental costs are computed in both cases, but they include different items.

Regarding the performance measurement, there is a decrease in the number of quantitative indicators reported by the companies. There is an obvious tendency in the reports prepared for 2013, when both companies were member of the IIRC Pilot Program Business Network, to focus on the narrative part. For instance, regarding the environmental KPIs, NN was declaring in 1998 nineteen quantitative indicators, while in 2013 it declared eleven quantitative indicators (Takeda is disclosing ten quantitative environmental indicators in the same year). The GRI guidelines G4, for instance, request for 34 environmental KPIs, of which 25 quantitative indicators. Both companies are applying the GRI guidelines.

In our opinion, a plus can be brought to the integrated reports by the balanced scorecard. Even though it was designed for internal purposes, it can be used for external reporting as well. The Balanced Scorecard views “organizational performance from four perspectives: financial, customer, internal business processes and learning and growth” (Kaplan and Norton, 1992). It links these measures to the company’s strategy through three principles: (1) cause-and-effect relationships, (2) performance drivers (i.e. leading indicators), and (3) linkage to financials (Eccles and Krzus, 2010). During the last decade the Sustainability Balanced Scorecard was developed. The Balanced Scorecard can prove that the requirements of internal and external stakeholders are interconnected. The linkage between external and internal reports is made in some of the last standards issued by IASB, too (for instance, in IFRS 8 “Operating segments”).

The most important change that sustainability should bring in a company is the one related to the improvement of the internal processes. The IIRC is referring to it as integrated thinking. As we already know, in many countries management accounting is outpaced by financial accounting. In the same time, sustainability will only be considered in the companies if it does not jeopardize the economic results. Thus, reporting is not enough; managers can continue to skillfully manage especially what they report externally, including the infusion of rhetoric and disguise (Hopwood, 2009). However, the change of the internal processes is highly depending on the production and use

\(^1\) Life-cycle Impact assessment Method based on Endpoint modelling.
of information. In the two companies analysed here we found evidence of the continuous improvement of their processes. For instance, in 2013, NN declares that it reached a point from where it became difficult to further improve and had to revise its standards. Also, “the company’s ambition to improve production performance has produced remarkable results, with cost of goods sold as a percentage of sales falling from 28% to 17% from 2003 to 2013”.

We consider that management accounting can pilot the changes in reporting. This offers opportunities to the management accountants, but they will have to face a heavy competition in this regard. Also, the integrated reporting will change the skills of the professional management accountants.

ACKNOWLEDGEMENT
This paper was co-financed from the European Social Fund, through the Sectorial Operational Programme Human Resources Development 2007–2013, project number POSDRU/159/1.5/S/138907 “Excellence in scientific interdisciplinary research, doctoral and postdoctoral, in the economic, social and medical fields – EXCELIS”, coordinator The Bucharest University of Economic Studies.

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Abstract: Due to globalization companies from different countries meet on the capital markets where investors try to place its temporary (whether short or long term) free capital. One of the main requirements affecting investors by decision-making is the evaluation of available information. When they decide to allocate their capital they require high quality information. The most coherent system providing detailed information about business events and transactions of a business entity is the accounting information system. The main output of each accounting system is a financial statements or annual report if required by accounting legislation. The accounting information obtained from such sources should be reliable, relevant, transparent and comparable. Comprehensibility belongs to the key characteristics of accounting information as well. To meet all interested user groups’ needs the financial statements must be prepared under the same rules applicable to all companies listed on the capital market.

Keywords: accounting systems, fair value, financial statements, financial decisions

1. INTRODUCTION

In the following article we will focus on fair value measurement applied for the reporting of assets used by the companies listed on the financial markets while preparing and presenting their financial statements.

2. ACCOUNTING SYSTEMS

Entities follow the effective national legislation regulating the preparation, form and content of financial statements. In the European Union (EU) and its member states the EU legislation is implemented. The EU base for accounting regulation is the Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards. By implementing of this regulation, the EU agreed that from 1 January 2005 International Financial Reporting Standards – IFRSs (along with the effective original standards known as International Accounting Standards - IASs) would apply for the consolidated financial statements of the EU listed companies. Nowadays, IFRSs are applied by all EU companies with
securities listed on a regulated market\(^1\), all other EU companies if they meet the size conditions stated by a member state where they were set up or if IFRSs option is applied by unlisted companies. An independent institution in London for more than 40 years has issued IFRSs. The IFRSs obligatory character in the EU is stated after their approval.

The number of IFRSs is not stable. Over time new issues, topics or market requirements cause their amendments, withdrawals or expansion. One of the issues that are addressed in the area of financial assets presentation is the fair value measurement. The fair value measurement belongs to challenging issues because it determines the value of assets presented in financial statements. This specific valuation concept has required the edition of a new separate standard – IFRS 13 *Fair Value Measurement*. The standard specifies the use of fair value in existing standards (e.g. in IAS 16 *Property, Plant and Equipment*; IAS 38 *Intangible Assets*; IAS 40 *Investment Property*; IAS 41 *Agriculture*) and clarifies fair value definition and its measurement application. Issue and effect of IFRS 13 has caused the amendments of the Act No. 431/2002 on Accounting in definition of fair value at the beginning of 2014. Although countries apply IFRSs on the voluntary basis or under the EU requirements in their national accounting legislation, there are still some differences. If we compare the German and Swiss legal system, we can determine following differences:

Due to the amendments to the German Commercial Code the incorporated changes were closer to IFRSs rules, including fair value as one of the particular basis of measurement, although the German accounting system is considered as a traditionally conservative oriented and based on Roman law. The principle of prudence and the bankruptcy is of key importance in order to protect the creditor.

The Swiss accounting system is essentially based on common law, principles in the form of recommendations for accounting and reporting (Swiss GAAP FER). Companies with securities listed on the Swiss stock exchange are required to apply IFRSs, respectively US GAAP. The annual financial statements shall be prepared under the concept of true and fair view. Financial events have to be presented reliably and without creative manipulation.

The following scheme presents differences between the accounting systems:

<table>
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<td>alle aus Unternehmen Beteiligten (insbes. Aktionäre)</td>
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<td>Informationsfunktion für wirtschaftliche Entscheidungen</td>
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Fig. 1. Survey of selected accounting systems. Source: Zorn, Markovič, 2013

3. FAIR VALUE

Comparability is one of the key features of financial information presented in financial statements that need to be met provided that the companies with securities listed on the capital markets use fair value measurement. Companies determine the value of assets and liabilities on the assumption of probable future economic benefits that the capital investment will bring to investor and not on historical costs, which were used as measurement base by the acquisition of assets. If an investor wants to make a decision on investment the information from financial statements is not enough, and because of this the investor must analyze quantity of additional data, which ultimately affect his final decision to invest free capital.

According to IAS 39 Financial Instruments: Recognition and Measurement financial assets with initial recognition as one(s) to be measured at fair value, with changes in fair value recognized in profit or loss, comprise those financial assets which have been acquired primarily for trading, such as:
- financial assets classified as held for trading;
- financial assets upon initial recognition designated by the entity as at fair value through profit or loss
- financial placement beyond insured measured at fair value through profit or loss.

According to IAS 39, financial assets are classified as held for trading at the time of acquisition when acquired or incurred principally for the purpose of selling or repurchasing it in the near term, if on initial recognition they are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking or they are a derivative (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument).

When an entity enters into contractual obligations through investment contracts then those contracts are financial liabilities recognized in statement of financial position. The investment contracts designated at initial recognition at fair value through profit or loss could be contracts concluded by the insurance company without discretionary participation feature (DPF) arising under the investment life insurance. Considering the fact that the assets held to cover liabilities arising from investment contracts are measured at fair value through profit or loss then revaluation of covered liabilities significantly reduces inconsistency in valuation (accounting mismatch). The inconsistency in valuation would occur if these financial liabilities were not recognized at fair value.

Changes in the fair value of financial liabilities arising from investment contracts are recognized in the statement of comprehensive income for the period in which they occurred, because the fair value of financial liabilities from investment contracts depends on the fair value of financial assets invested. The fair value of financial liabilities is derived from the fair value of the respective asset both at initial recognition and at the date on which the financial statements are prepared.

4. FAIR VALUE MEASUREMENT

Although the rules for the recognition and measurement of financial assets and financial liabilities are stated in IAS 39, it should be noted that IFRS 13 sets out the requirements for measuring the fair value of a financial asset or financial liability, whether by designation or otherwise, or whose fair value is disclosed.

According to IFRS 13 fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

In case of financial instruments measured at fair value, the fair value is based on quoted market price for those financial instruments traded in an active market if such a price is available. The market is considered as active if quoted prices are quickly and regularly available and represent actual and regularly conducted transactions on an arm's length commercial relationship between
independent parties. If the market for a financial instrument is not active, an entity establishes a fair value by using valuation techniques.

5. FINANCIAL STATEMENTS USED FOR FINANCIAL DECISIONS

The technique for valuation of a dividend is based on the theoretical share price. On the basis of the ex post analysis investors can affect their investment decisions in the future. Investors reinforce their decisions based on ratio analysis. As an example the following graph shows development of Volkswagen’s share price in the period 2008–2013:

![Fig. 2. Development of Volkswagen’s share price](source: Zorn, Markovič, 2013)

The historical analysis shows that the data can be interpreted as a reference and their performance can be estimated in the future. In accordance with the ex ante analysis investors try to forecast the future to avoid bankruptcies and to timely recognize the need for action in order to prevent financial problems.

6. CONCLUSIONS

Before financial decision making, investors must take into account the accounting systems, which generate information for subsequent analysis. Regulatory body in each country affects accounting system. The prudence concept can be applied on varying degrees and this fact could cause difficult interpretation of the disclosures.

It is an advantage for investors if all companies in which they intend to invest are using the same accounting rules, such as is a set of IFRSs. IFRSs accept the fair value as a measurement basis. Despite the fact that companies follow the same definition, the application in each country is different, mostly because of its own interpretation and application. While national legislation in the Slovak Republic applies all measurement basis based on prudence convention, German legislation promotes the principles of valuation based on historical cost. The fair value represents ideally the market value obtained as a result of supply and demand assuming the existence of an active market. In case the active market does not exist, the company must proceed to determine fair value based on the application of the fair value hierarchy recommended by IFRS 13 Fair Value Measurement.

From the perspective of investors the advantages of the fair value measurement are as follows:
- In the financial statements entities present assets and liabilities at values that are comparable to market prices at a given time and more accurate than the value that would be determined using historical cost,
- The valuation method limits the ability of companies to manipulate with their net income because the expenses and revenues from revaluation of assets and liabilities are recognized in the period in which they arise and not at date when they are realized as a result of the transaction.

Fair value measurement increases the transparency of reported information and it will improve the consistency and comparability of financial information. To be objective, it is necessary to mention also disadvantages of fair value measurement:
- The fair value hierarchy gives the highest priority to the quoted price, but in practice it may happen the quoted price is not available. In such case the fair value hierarchy prescribes selection of appropriate valuation technique that could be based even on estimates, e.g. discount rate,
- Users of financial information from financial statements have in some cases problems to differentiate the objective data based on current quoted prices from subjective data based on estimates underlined by hypothetical calculations. This problem can be minimized by accurate and detailed description of the fair value determination in the notes to the financial statements.

To sum up, the more detailed information about valuation, measurement, recognition and presentation in financial statements of companies the more accurate information base for investors available for their investment decision-making.

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Grant: VEGA Nr. 1/0008/14: Key trends in managers’ financial decision-making process under conditions of unstable financial markets
LINGUISTIC QUALITIES OF FINANCIAL STATEMENTS IN POLAND: PREPARER AND USER PERSPECTIVE

Karol Marek KLIMCZAK
Kozminski University
kmklim@kozminski.edu.pl

Anna Marta PIKOS
Kozminski University
apikos@kozminski.edu.pl

Abstract: The goal of this paper is to explore the use of narratives in financial statements prepared in the Polish language. We use genre analysis and compare financial statements with management reports to contrast the two genres and describe the interconnections between them. The paper contributes to a growing body of research concerning the communication strategies used by preparers, the interpretation strategies of the users and the effect of linguistic qualities on the value relevance of accounting numbers. Extant literature concerns only statements written in English languages, while the continental European languages remain unexplored. The study of Polish language communications is valuable, because Polish shares a number of characteristics with Russian, German, French and other continental languages. We focus on notes concerning goodwill impairment tests because the communication of judgments involved offers a challenge. We found that the factual style, avoidance of evaluative terms and deixis are the distinguishing characteristics of financial statements. In contrast, management reports contain a variety of strategies, including a liberal use of evaluation and deixis. Preparers of financial statements seem to be discouraged from discussing potentially significant, negative factors. The study of connections between the two reports shows that the negative factors can be identified in the management reports, following hints left by the preparers, but this is possible only for professional users.

Keywords: financial information, financial statements, narrative reporting

1. INTRODUCTION

Accounting is associated mostly with numbers, but narratives begin to play an increasing role in the communication of financial information concerning stock-exchange listed companies. First of all, the International Financial Reporting Standards require companies to disclose a variety of descriptive information in addition to the core financial statements. Secondly, every annual financial statement is accompanied by a management report, which is required by the new accounting directive of the European Union (2013/34/EU). The scope of the management report is broader than that of the financial statements, as it includes non-financial performance indicators and a discussion of strategy, but it must be aligned with the financial statements. Thirdly, the need for stronger narrative reporting is recognized as an element of rebuilding the trust in financial markets. The narrative reporting reform in the United Kingdom is a good example of this trend.

The goal of this paper is to explore the use of narratives in financial reporting in the Polish language, thus extending the studies of English language narratives to the languages of continental Europe. The Polish language shares certain characteristics with major continental languages, such as Russian, German or French. For example, all of these languages use verb conjugation, while English does not. Polish financial statements are an interesting subject in themselves, because the stock market and accounting regulation has changed dramatically over the past twenty years and further changes can be expected to occur as the Polish economy integrates with the global markets. We attempt to study the language of financial statement narratives, by placing them in the context...
of the management report and analyst recommendations, complementary sources of information. The advantage of this approach is that we exploit both the contrasts between various sources of financial information and the interconnections between them. This has been done in earlier research, which pointed to differences between the discourses found within the financial statements: “the accounting discourse tends to report accurately and factually on the basis of financial evidence about the past corporate performance, whereas the chairman's letter is meant to promote a positive image of the company to its shareholders and other stakeholders in order to sustain their confidence in future corporate performance” (Jones, 2014, pg. 90).

Early research into the use of language in financial statements focused on their readability, finding that the statements of well performing companies were easier to read (Subramanian, Insley, & Blackwell, 1993). It is the application of research methods from linguistics that brought a fresh perspective on the topic. Language pragmatics research looked at the use of words and phrases such as however, as a result and additionally, which are associated with discourse connectedness and allow writers to modify the evaluations of the readers by, for example, highlighting a positive result or offsetting a negative result in the case of however, or building up a series of positive results in the case of additionally (Crawford Camiciottoli, 2010). Similar studies lead to the development of analytical methods, which help uncover manipulation and fraud in accounting texts. Humphreys et al. (2011) find that fraudulent management reports tend to exhibit characteristics of crafting, such as the use of activation language, complex words and sentences, imagery words, pleasantness and as a result the language is less diverse than that of non-fraudulent statements. A study of 10-K statements (Goel & Gangolly, 2012) found that fraudulent statements tended to contain more passive voice, more adverbs and more uncertainty markers.

In our exploration of financial statement narratives, we use the method of genre analysis. A genre is commonly defined similarly to the Webster's New Encyclopedic Dictionary as “a category of artistic, musical, or literary composition”, which points to the traditional view of genre analysis as the study of the context, communicative aim, form, style and content of narratives, which aims to find commonalities between narratives of a given genre and differences in comparison to other genres. Genre analysis has been used in the analysis of professional discourse in order to explain why professionals use language the way they do (Bhatia, 1993). As Bhatia writes in a later work, “professional discourse seems to operate simultaneously at four somewhat distinct and yet overlapping levels, or concepts of space, identified as discourse as text, discourse as genre, discourse as professional practice, and discourse as professional culture” (Jones, 2014, pg. 76).

Swales (1990, pg. 33) notices, that the term genre analysis can be used in an array of approaches. From a literary perspective genres can be viewed as forms of expression which persist over time and are recognised by readers as distinct. Jameson (2000) refers to structuralist theories of communication, which look at narratives as cultural artefacts, amenable to analysis. However, she also discusses the phenomenological perspective, in which the reader's interaction with the text is the focal point. In a manner, this perspective can be linked to sociological approaches to genre analysis, which rely on the readers' perception of texts, their form and meaning (Swales 1990, pg. 35). Finally, the methods of linguistics can be coupled with critical philosophy in the form of critical discourse analysis, which aims to uncover the motivations hidden behind the words (Bhatia, 2012).

The structuralist, phenomenological and critical perspectives illuminate the problem of narratives in financial statements from different angles. Taking the structuralist view first, it is clear that financial statements rely on defined methods of classification and measurement, which constitute the fabula. Finance professionals would agree, that the same set of accounting numbers can be viewed in various ways, hence creating the potential for many stories to be developed. Then, the process of writing the stories in the report can yield a variety of texts concerning the same story. Taking the phenomenological viewpoint, one can easily imagine, that the users of financial statements can interpret the narratives in various ways depending on their experience, an observation which is recognised by standard-setters and regulators who develop disclosure requirements. The critical perspective brings the power struggles between corporations and their stakeholders into the spotlight, in an attempt to explain why financials statements are written the way they are.
Bhatia (2004, pg. 23) summarizes the elements of a genre, which are common among the major theoretical perspectives:

1. genres can be recognized by members of the professional community as communicative events, which serve specific purposes and occur regularly,
2. genres are subject to conventions which constrain the intentions one can express, the form and style which can be used,
3. the members of a given professional community are able to understand the use of genres better than outsiders,
4. professionals exploit various resources to express their intentions beyond those specified by conventions,
5. genres reflect professional and organisational cultures,
6. each professional genre has integrity of its own.

In our analysis of financial statements as a genre, we look at the context, form, style and content of elements pertaining to goodwill impairment testing. We focus on statements which signal uncertainty or manipulation and contrast them with the content of the management report. At the same time, we explore the pragmatic strategies used by the preparers, which allows us to compare corporate disclosures with findings of a previous study of Polish analyst recommendations (Dynel & Klimczak, 2014).

2. THE REGULATORY CONTEXT

Unlike the developed markets which evolved over much of the twentieth centuries, the Polish stock market needed to be created from basics after the fall of communism in 1989. The new national accounting law was initially created with the purpose of increasing tax revenue and serve the needs of creditors, rather than those of investors, which was a response to the concerns associated with the turbulent development of the free market in the initial stage. The future of the Polish accounting regime was uncertain at the time (Jaruga, 1993). It wasn't until 1991 that the Warsaw Stock Exchange began operations with 9 companies listed initially. In subsequent years, the dynamic development of the capital market was accompanied by rapid regulatory adjustments (Dobija & Klimczak, 2010). The number of listed companies exceeded 200 in the year 2000, while in 2013 there were 459 companies listed in the main market and a similar number listed in the alternative market called NewConnect, positioning the Warsaw Stock Exchange as the leading market in the region. In 2004 Poland joined the European Union, and adopted EU regulations, including the requirement for consolidated financial statements to be prepared in accordance with the International Financial Reporting Standards (Grabinski, Kedzior & Krasodomska, 2014).

The Warsaw Stock Exchange can be described as a tightly regulated market, a characteristic to which its success is often attributed (Stringham, Boettke & Clark, 2008). The main act regulating companies whose shares are traded in a regulated market in Poland is the Act of Parliament (29.07.2005), which incorporates EU directives. Reporting requirements are set in the Regulation of the Minister of Finance (19.02.2009), which enumerates the required contents of annual, semi-annual and quarterly reports but allows companies to include additional information. The required elements are:
1. A letter from the CEO, commenting on the results and future perspectives,
2. Selected financial data, including comparable data for the past year, in PLN and EUR,
3. The annual financial statements, prepared in accordance with the IFRS or Polish accounting standards,
4. The management report, the contents of which are also enumerated in the regulation,
5. An attestation of the management board as to the reliability of the report,
6. An attestation of the management board concerning the selection of the auditor,
7. The audit report.
We interviewed one preparer and one financial analyst to determine what is their perception of the context of financial reporting. Both interviewees agreed, that the financial statements and the management reports are highly regulated, and much of their content is not relevant to users. They acknowledge that the two documents are prepared in different ways. The financial statements are written in accordance with accounting standards, thus perceived as technical. The users focus is mostly on quarterly income statements and working capital sections of the balance sheet, which allow analysts to forecast future cash flows. Users rely on their experience to identify questionable figures, then they use the notes to financial statements to investigate further. The interviewees agreed that the management report is less relevant. It is prepared by public relations or investor relations personnel, who are expected to bias the review towards the positive. The regulated content includes large amounts of irrelevant, generic statements. While these may be useful to a new user, seasoned users, who already know the company, have little use for them. The only exception is operating data concerning production or sales, which is not included in the financial statements. Management reports do not contain forecasts for legal reasons. Communications issued by companies are verified against other information sources and the experience of users.

3. FINANCIAL STATEMENT NARRATIVES

Financial statements of large, stock listed companies contain over a hundred pages of text and tables, which lead us to select one element to make our analysis feasible. In this section we focus on notes concerning tests for the impairment of goodwill resulting from business acquisitions, while in the next section we explore the elements in the management report, which refer to the business units subject to impairment testing. All through the analysis we use the 2013 consolidated financial statements and management reports of companies listed at the Warsaw Stock Exchange. We select large companies, included in the WIG30 index, so that we can assume they allocate sufficient resources to the reporting processes. There are nine companies, other thank banks, which report goodwill in their assets: Asseco Poland, Grupa Azoty, Boryszew, Cyfrowy Polsat, Energa, Eurocash, Kernel, Tauron, and TVN.

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<td>4.77</td>
<td>0.30</td>
</tr>
<tr>
<td>Energa SA</td>
<td>Conventional Electricity</td>
<td>2 152</td>
<td>2 757</td>
<td>4 121</td>
<td>2.26</td>
<td>52.82</td>
</tr>
<tr>
<td>Eurocash SA</td>
<td>Food Retailers &amp; Wholesalers</td>
<td>1 178</td>
<td>3 989</td>
<td>1 164</td>
<td>-0.23</td>
<td>-24.10</td>
</tr>
<tr>
<td>Grupa Azoty SA</td>
<td>Specialty Chemicals</td>
<td>1 790</td>
<td>2 369</td>
<td>2 403</td>
<td>38.35</td>
<td>88.02</td>
</tr>
<tr>
<td>Kernel Holding SA</td>
<td>Farming &amp; Fishing</td>
<td>525</td>
<td>2 150</td>
<td>1 820</td>
<td>29.63</td>
<td>-23.83</td>
</tr>
<tr>
<td>TAURON PE SA</td>
<td>Conventional Electricity</td>
<td>2 145</td>
<td>4 615</td>
<td>7 805</td>
<td>-22.68</td>
<td>-10.24</td>
</tr>
<tr>
<td>TVN SA</td>
<td>Broadcasting &amp; Entertainment</td>
<td>1 191</td>
<td>375</td>
<td>941</td>
<td>-1.87</td>
<td>0.77</td>
</tr>
</tbody>
</table>

Fig. 1. Overview of the companies studied [EUR million, %]. Source: Infinancials.

The description of goodwill impairment tests is an interesting research object. First of all, companies do not disclose their calculations, only the conclusion of the test, often without any numbers. The user of financial statements needs to rely on the narrative, whereas most of the financial statement information comes in the form of numbers. Secondly, the tests themselves are associated with significant uncertainty and require professional judgement, because they rely on forecasts of future performance, whereas most of the financial statement information is set in the
present or the past. Thirdly, if the result of the test is negative, goodwill must be impaired, resulting in a significant reduction of earnings. Goodwill recognition under IFRS 3 relies on the concept, that a price paid, i.e. the total consideration, in a business acquisition can be assumed to represent the underlying value of the acquired business. If the reporting company is unable to allocate the premium over the book-value to specific assets, goodwill is recognised as the difference between the purchase price and the fair value of acquired assets. Goodwill can be perceived as the present value of future profits resulting from the acquisition. Reporting companies are required by IAS 36 to test annually if the future profits, i.e. the recoverable amount, are in fact greater or equal to the carrying amount of goodwill.

The preparers of financial statements face a difficult task when they need to communicate the results of goodwill tests. On the one hand, their professional ethics requires that the test results be reliable. On the other hand, they must be aware of the inherent uncertainty and potential suspicion of the financial statements users, who may assume the preparer's modify the test results to avoid an impairment. In fact, of the companies studied here only TVN reported an impairment of goodwill in recent years, but it was not a result of impairment testing. TVN sold its wholly owned online business Grupa Onet.pl in 2012 for a price below the book-value.

The format of the descriptions of goodwill testing is predictable. They contain elements of accounting policy referring to goodwill, a description of the key assumptions and methods used in the tests and the conclusions. The degree of detail in the descriptions varies greatly. Most companies do not report the recoverable amounts that is the amounts calculated as part of the test. Grupa Azoty is the only exception. Preparers state that they have carried out sensitivity analysis in Tauron, Energa and Asseco Poland. Only Asseco Poland presented the results of sensitivity analysis concerning the assumed discount rates and growth rates.

The descriptions of goodwill testing are written in a factual style, avoiding adjectives, adverbs and other signals of evaluation (Hunston & Thompson, 2000, pg. 1–27). Preparers use the depersonalization strategy, which allows them to detach themselves from the text, rendering the text more objective, but also reducing the responsibility of its authors (Martín-Martín, 2008). It is achieved by using the word Group as the subject or omitting personal pronouns, which is possible in the Polish language by using verb conjugation, rather than resorting to passive voice. For example, in the statement of Kernel we read that “the Group reviews its subsidiaries” [“Grupa dokonuje przeglądu poszczególnych jednostek”], and in the statement of Energa we find that “the Group carried out impairment testing” [“Grupa przeprowadziła test na utratę wartości”]. When the results of judgments are communicated, however, preparers resort to the impersonal as in the statement of Eurocash, where we find that “as a result of the effected analysis, it is confirmed an impairment is not required” [“w wyniku przeprowadzonej analizy potwierdzono brak konieczności dokonania odpisu aktualizującego z tytułu utraty wartości”].

Alternatively, judgments are attributed to the management, especially when the assumptions of tests are concerned, which may be a signal of subjectivisation. The subjectivisation strategy allows the preparers to express a judgment as the personal perspective of the management, rather than an objective fact (Martín-Martín, 2008). The following excerpt from Kernel is indicative of this strategy:

*The management believe, that any possible changes in the key assumptions, on the basis of which the recoverable amount was calculated (...), would not cause a situation in which the book their value would exceed the recoverable amount.* [Kernel]

*Kierownictwo uważa, że wszelkie możliwe zmiany w kluczowych założeniach, na podstawie których wyliczono kwotę odzyskiwalną (...), nie spowodowałyby sytuacji, w której ich wartość księgowa przekroczyłaby wartość odzyskiwalną*

These statements seem puzzling, given that no sensitivity analysis is performed in most cases. Sometimes the statements attributing judgements to the management are particularly awkward, as in the case of Boryszew:
A change of factors is not probable (...). The Management believe that even if justified and probable changes in the key assumptions took place, (...) the book value (...) would not exceed the recoverable amount. [Boryszew]

[Nie jest prawdopodobna zmiana czynników (...). Zarząd (...) uważa, że nawet gdyby zaszły uzasadnione i prawdopodobne zmiany w głównych założeniach (...), to wartość bilansowa (...) nie przekroczyłaby jej wartości możliwej do odzyskania.]

This statement may have been crafted by the auditors of Boryszew, which would explain its unusual style, but the reader may nevertheless wonder which changes are of concern. Is it the probable ones which are claimed not to exist, or the improbable ones, which can occur? How is it then, that even improbable changes would not cause changes in the results of impairment tests? We can demystify these statements by examining the management reports.

4. MANAGEMENT REPORT NARRATIVES

Management report narratives are structured and formatted in various ways, even though the minimum content is prescribed by law. The documents are about 100 pages long, with the majority of the document devoted to mandated content, written in a technical manner, with repetitions, as the same events require disclosures under various headings. Asseco Poland and Eurocash prepared graphical documents, using colours, graphs and creative formatting, with the main points communicated clearly at the beginning and mandated content placed in the latter parts of the document. TVN, a media company, prepared a consistently formatted document, but refrained from using graphics. The other companies formatted their reviews following the content requirements of the law, with many detailed subsections. Surprisingly, two companies did not include a table of contents. The style varies from factual and impersonal, similar to financial statements, to personal and speculative. Evaluation is present in the use of adjectives and adverbs. In some cases the style is impersonal, the word Group is often used as the subject, but the personal pronoun “we” is just as common, which signals subjectivisation.

Interesting differences appear in the style of the documents, which we describe below in reference to goodwill testing. None of the companies studied here impaired goodwill in 2013 or earlier years. The only exception is TVN, which impaired goodwill resulting from the acquisition of Grupa Onet.pl in 2012. This was a result of sale of 75% of shares below their book-value, not impairment testing, but the way the impairment is explained in the management report can help reveal the motivations of the preparers. There are many passages devoted to this topic in the 2012 annual report describing the technical details of the transaction, but the passage below is the first one to appear:

After the sale of the shares in Grupa Onet.pl to Ringier Axel Springer (...) we lost the control over our online business dominated by Onet (...) Both transactions are perceived by the TVN Group as long-term investments, the goal of which is (...) the development of the online market (...) through the use of economies of scale and synergies resulting from the cooperation with our strategic partners. [TVN 2012]

[Po sfinalizowaniu sprzedaży akcji Grupy Onet.pl do Ringier Axel Springer (...) straciśliśmy kontrolę nad naszym biznesem online zdominowanym przez Onet (...) Obie transakcje są postrzegane przez Grupę TVN jako inwestycje długoterminowe, których celem jest (...) rozwijanie rynku online (...) poprzez wykorzystanie efektów skali i synergii wynikających ze współpracy z naszymi strategicznymi wspólnikami.]

The sale of Grupa Onet.pl is thus portrayed as a positive event, an investment, despite the fact that TVN sold 75% of its shares and used the proceeds to retire debt. This is a creative element, a play
of words, because the term investment refers to the classification of the remaining 25% of shares in Grupa Onet.pl as “investments in associates”, rather than the common meaning of the term. Further, TVN reports a “corrected” EBITDA in the discussion of financial performance, from which it excluded the impact of the goodwill impairment. The difference is significant, because the reported EBITDA was negative, while the corrected one is positive, even if low.

Since no other companies impaired goodwill in 2013, the next most interesting settings are cases, where uncertainty concerning impairment testing is the greatest. Boryszew, which we discussed in the previous section as an example of an awkward disclaimer, is one of such cases. Boryszew allocated the largest amount of goodwill to its German subsidiaries, especially Theysohn Kunststoff GmbH and Boryszew Kunststofftechnik GmbH. There is already a hint in the financial statements, that growth of sales in these companies is of concern, because there the note states, without any explicit reason, that the acquisition of new contracts is seen as probable. Little discussion of these subsidiaries can be found in the management report, until one notices, that those companies are included in Boryszew Automotive Plastics Group, or BAP, which is in turn included in the Automotive segment, the results of which are discussed in the document:

Lower sales were associated with a decrease of demand in the European automotive industry and lower sales as a result of contractual discounts and the contract lifecycle. In 2013 old contracts gradually expired and were not being (...) replaced (...). In the case of BAP Group companies we expect, that [the situation will improve] in mid 2015. [Boryszew]

Overall, the discourse in the management report is less factual, and refers to expectations, while the descriptions of impairment testing referred to assumptions. In the financial statements, the concern was that the assumptions may change in the future, but in the management report the preparers discuss their hopes for the future. This difference is quite clear in the case of Asseco Poland. In the financial statements one finds a table with the results of sensitivity analysis, containing the assumed discount rates and growth rates, and a comparison with the critical rates beyond which impairment would need to be recognised. The figures presented in the table are not discussed, but it is clear that the safety margin is the lowest for Matrix IT Ltd, a major subsidiary. The commentary in the management report regarding Matrix IT Ltd reveals the underlying causes, but the preparers make an effort to situate these problems in the past and to use positive words when referring to the present. This is a typical example of deixis, a strategy aimed at framing the perspective of the reader (Hanks, 2009):

The year 2013 was challenging for the company, mostly because of economic slowdown and postponement of IT investments by clients. (...) In the fourth quarter of 2013 the company had to write down receivables of NIS 2 million because of the bankruptcy of two clients in the Israeli market. Despite the aforementioned difficulties Matrix IT managed to maintain its strong market position and strengthen its core operations, i.e. the sale of own software (...). [Asseco Poland]
Perhaps the management report should be treated as another story, or another voice in which the same underlying facts and events are used as the fabula. When we read the report of Eurocash, we find no signals of uncertainty in the financial statements. The note is brief and technical, no sensitivity analysis is performed. The two largest amounts of goodwill are associated with the Tradis Group, a major FMCG distributor, and the Premium Distributors Group, which trades alcohol products. Both groups experienced a decrease in sales revenue, but the negative events are put firmly in the past, while positive events are reserved for the future, another example of time deixis. The decrease in sales resulting from the loss of a major client is removed from the historical growth rate calculations, and the reader’s attention is refocused on “continued sales”:

The main reason for the lack of dynamics in sales was the market situation and internal factors associated with the acquisition and the consolidation process of Tradis. (...) The decrease of sales of Tradis was caused by the withdrawal from sales to the Stokrotka network (...) Taking into account only continued sales, Tradis experienced an increase of 1.6%. (...) The full synergy effects (...) will be possible to achieve within 3 years of acquisition. [Eurocash]

[Głównym powodem braku dynamiki sprzedaży były trudne warunki rynkowe oraz czynniki wewnętrzne związane z przejęciem i procesem konsolidacji spółki Tradis. (...) Spadek sprzedaży Tradis spowodowany zaprzestaniem sprzedaży do sieci Stokrotka (...). Biorąc pod uwagę jedynie sprzedaż kontynuowaną, Tradis odnotował wzrost o 1,6%. (...) Pełne efekty synergii (...) będą możliwe do osiągnięcia w ciągu 3 lat od przejęcia.]

5. CONCLUSIONS

We explore the use of narrative in the notes to annual financial statements concerning goodwill impairment testing in the Polish language. We found that the narratives adhere to a common structure and use similar communicative strategies. They are written in a factual, impersonal style, avoiding the use of evaluative terms, and the use of depersonalisation is common. Exceptions to the rules exist in the form of statements communicating judgements attributed to the management. In contrast, management report narratives are often written in a personal style, use evaluation freely. Their authors use strategies aimed at modifying the perspective of the reader, such as redefining terms, or placing negative events in the past. However, the differences between the two reports are not as deep as one might expect, because both reports are regulated and contain large amounts of information which is of little interest to the majority of users. For example, two of the companies we studied failed to include a table of contents in the reports, which may signal that they treat reporting as a compliance exercise, not a communication event.

When we compare the findings to our previous study of financial analysts (Dynel & Klimczak, 2014), we come to the conclusion, that analytical reports represent the most creative use of language. Evaluation is the main communicative aim of their reports, whereas corporate disclosures are expected to provide information, biased as it may be. While there are parallels between analyst reports and management reports, such as the use of subjectivisation and deixis, analysts use hedging strategies to a much greater extent. This is of course partly explained by the regulatory context, because the content of management reports is regulated and the documents are of much greater length than analyst reports. Interestingly, the preparers of financial statements appear to detach themselves from evaluation, even in cases where evaluation is in fact called for by the accounting standards.

Our analysis of interconnections between financial statements and management reports reveals that the narratives in financial statements contain hints that can lead a professional reader to
discover information, which is not explicitly communicated. In particular, it appears that the preparers of financial assume a professional reader will be able to read between the lines, and refrain from communicating negative information about the company. This can be explain by their reliance on a factual style. Negative information included in the financial statements, even in a note, becomes a fact, whereas the same information included in the management report is only a story. The cases we examined do not appear to involve fraud or potential financial distress, but the omission of potentially significant negative signals leads ask to form the question about how the integrity of the financial statements and their preparers is defined by the professional community.

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BIBLIOGRAPHY


CORPORATE SOCIAL RESPONSIBILITY – PROBLEMS OF AMBIGUOUS STANDARDS AND INDEX FOR EVALUATION: SOME PRELIMINARY NOTES

Sarka KOCMANOVA
University of Finance and Administration
sarka.kocmanova@centrum.cz

Irena JINDRICHOVSKÁ
Anglo-American University, Prague
irena.jindrichovska@seznam.cz

Abstract: The goal of this paper is to determine problems in finding an objective measure for evaluation of reports on activities of corporate social responsibility. In recent years we have seen a rapid increase in accountability and responsibility reports, particularly in large global companies. The increased call for transparency shows some potential convergence in social terms of the topic. Tencati et al. (2004) note what their American colleagues perceived this pressure at the end of the last century – as there was no single, shared, and the internationally accepted standard for assessing the socio-business issues. On the contrary, the authors noticed that a large number of different approaches and initiatives developed. Their detailed description goes considerably beyond the objective of this paper. We will therefore only briefly introduce the most important ones: Standards in the field of CSR Fombrun states in its list of the most important standards and certification touching the various points of view the issue of CSR. They are SA 8000 Workplace / Employee Relations, ISO 9000 Organization & Governance, ISO 14001/14004 Environment, AA 1000 S Stakeholders. There exist reports on Global Reporting Initiative (GRI) based on publicly available information in annual financial reports, stand-alone Corporate Responsibility reports on company websites, which encompasses all sectors of CSR. In this article we attempt to unveil the appropriate standards for measurement of social responsibility in qualitative items.

Keywords: corporate social responsibility, reporting standards, evaluation reports, transparency

1. THE INTRODUCTION

In the Czech Republic there are several approaches to CSR reporting. A lot of them are coming from the general financial reporting and are used mainly in international companies. Evaluation system of social responsibility in the Czech Republic has a number of “regulating” entities, such as the Czech Society for Quality, Business Leaders Forum (BLF), the Czech Office for Standards (ISO 26000), The Czech Chamber of commerce, Fair Business Association and the Association for the prize for quality of the Czech Republic. Each of these regulators has focused on different part of CSR:

- BLF seeks to maximize the spread of awareness of CSR,
- The Czech Society for Quality provides education in this field and
- Fair Business Association in cooperation with the National Quality Policy of Czech Republic deals with the evaluation of company results in this area.

Support of CSR in Czech Republic is also connected with cooperation of International companies, such as ILO (International Labour Organization) and the OECD (Organisation for Economic Co-operation and Development).
This article examines the differences between the form and attitude to CSR on the sample of 25 Czech companies using behavioural analysis. In this vein this study focuses on evaluation of reporting systems based on the local Czech rating system of Corporate Social Responsibility (KORP). The principal method that we intend to use is a local Czech rating system of Corporate Social Responsibility, which was created by the Fair Business Association in cooperation with the Association for Quality Prize of the Czech Republic. It is a national method for evaluating CSR practices. The Czech model of evaluation of CSR reporting (KORP) originates from the assumptions using.

- GRI (Global Reporting Initiative)
- Model EFQM Excellence (European Foundation for Quality Management) and
- CAF (The Common Assessment Framework)

In the case of non-profit organizations the system operates on a different principle. The non-profit companies in each period continuously monitor the balance of income and expenditure.

The ideal approach to CSR could be found somewhere between the two different approaches (profit and non-profit). And such approach is in fact becoming more common. Firms are generally more willing to take responsibility for their public affairs and contribute to solve social problems.

The main aim of the study:
The primary goal of the study is to provide an overview of how companies in the profit and non-profit sectors report on sustainability aspects of their business using the local model (KORP) guidelines, specifically the Deming Cycle – PDCA. The overview highlights the differences in how the various companies report on the gaps where no (or few) companies report, and seeks to investigate why companies do or do not report on certain indicators. Reporting on CSR is an important issue for the European Social Partners in different branches according to their joint 2011 – 2013 statement on CSR.

Research questions
For each of the selected Czech companies, the present study aims to answer the following research questions:
1. Does the company use the GRI Guidelines or local Czech rating system of corporate social responsibility (KORP)?
2. Does the company use the Triple bottom line approach?
3. Does the company use a Code of corporate social responsibility?
4. Has the 2011–2013 report been externally verified and has the application level been checked?
5. What general gaps in CSR reporting can be found and what are the reasons for such gaps?

2. PREVIOUS AND CURRENT SYSTEMS OF MEASURING THE CORPORATE SOCIAL RESPONSIBILITY

Aupperle, Carroll and Hatfield (1985) in their research admit the need for new qualitative approaches to assessment of "unfathomable benefits" resulting from CSR and wondered whether problems related to CSR profitability will ever be completely resolved.

Tencati et al. (2004) note that there is no single, shared, and the internationally accepted standard of assessing the socio-business issues. On the contrary, they notice that large number of different approaches and initiatives has developed. Their detailed description exceeds the objective of this work and therefore we will only briefly recapitulate the most important:

Fombrun (2005) provides a list of the most important standards and certification touching the various points of view the issue of CSR:

- SA 8000 Workplace / Employee Relations (as the name implies, is focused on the working conditions of employees in accordance with the ILO and other international conventions).
- ISO 9000 Organization & Governance (Quality Management System).
- ISO 14001/14004 Environment (Environmental Management System).
- AA 1000 S Stakeholders (based on a process approach, with the aim of transparency in communication with each stakeholders group, but not the performance standards).

In these four major standards one can notice that each of them covers only particular area of CSR. AA 1000 S deals with the issue of CSR standards with the widest-ranging problem. It focuses only on the processes leading to the achievement of desired social performance. SA 8000 and AA 1000 S cannot be regarded as competitors due to their different objectives and scope and can be used in combination. The same can be said of other ISO standards. The problem remains the fact which we already indicated above. The Italian authors Tencati et al. (2004) state that the number of different standards capturing different angles makes comparing the performance of companies in the field of CSR rather complex. Certain way out then appears the standard ISO 26000, which sets ambitious goal to be the unifying element that will assist organizations in realizing their social responsibilities while respecting the diversity of cultural, social, environmental, legislative and economic conditions. ISO 26000 provides guidance rather than requirements, so it cannot be certified unlike some other well-known ISO standards. Instead, it helps to clarify what is understood by the social responsibility. It helps businesses and organizations to translate principles into effective actions and shares best practices relating to social responsibility globally. It is aimed at all types of organizations regardless of their activity, size or location.

The standard ISO 26000 was launched in 2010 following five years of negotiations between many different stakeholders across the world. Representatives from government, NGOs, industry, consumer groups and labour organizations around the world were involved in its development, which means that it represents an international consensus. In addition to providing basic guidelines relating to the operationalization of CSR, identification and involvement of the different stakeholders and enhancing credibility of reports, announces the emphasis on the evaluation of performance and progress. Its implementation, however, can be considered as time-consuming, thus only time will tell what is its contribution to the unification of CSR standard evaluation.

Steinweg and Wilde-Ramsing (2012) of SOMO (Centre of Research on Multinational Corporations) presented the study entitled “the Use of the Global Reporting Initiative (GRI) in Sustainability Reporting by European Electricity Companies”. This study investigated the CSR reporting of nineteen European electric utility companies on ten GRI and EUSS labour related indicators. Their research indicated interesting findings. The analysis of Steinweg, Wilde-Ramsing revealed that more than 60% of the claims of ‘full’ reporting on the CSR indicators included in this study are at least partly false or misleading.

They founded discrepancies in 10 out of the 12 corporate reports that had been externally assured or checked by the third party auditor or the GRI itself. Actually, some of the reports with the most discrepancies were externally verified and checked at the highest level possible“A+” . These results call into question the credibility of the assurance system associated with the GRI Reporting Framework. The findings do not exactly clarify the results, because the discussion about the effectiveness of voluntary versus mandatory approach to corporate accountability and corporate responsibility is a long and complex approach. They recommended to improve the clarification, specificity and relevance of the indicators of CSR reporting requirement and concluded that the voluntary initiatives should be codified and credible.

Publishing reports of socially responsible companies became lately a phenomenon showing a strong and increasing trend. This has been confirmed by the international advisory and audit firm KPMG. KPMG researches the topic of CSR reporting since 1993 and it shows the results of research
carried out in year 2008 on a sample the world's largest companies - top 250 according to the Global Fortune for year 2007 (G250) and the 100 largest companies by turnover achieved (N100) in 22 different countries, among which the Czech Republic was included for the first time just last year. In our research we use the specification and standard based on a Survey of Corporate Responsibility Reporting by KPMG 2013\textsuperscript{22}.

In this proposed research project the quality of company’s reports in profit and non-profit sector will be assessed using seven standards based on KPMG classification, in particular:

1. Strategy, risk and opportunity,
2. Materiality,
3. Target setting and relevance of indicators,
4. Suppliers and the value chain,
5. Stakeholder engagement,
6. Governance of Corporate Responsibility and

In this area we also meet with a number of experiments of different organizations using different standards in order to assess the social performance of companies. The most important indexes dealing with the performance of companies are used on global stock exchanges. But these indexes in order to assess various CSR or sustainable development in its portfolio include only those companies, which have good economic results derived from stock market indices. It may therefore happen that we do not include those companies which lead to achieving a high level of social responsibility, but are not present in the evaluated sample due to worse economic performance.

The most famous example of such an index is the Dow Jones Sustainability Index (DJSI)\textsuperscript{23}. It is a member of the large family of indices, and it is based on the evaluation of economic, environmental and social criteria drawing up a "Corporate Sustainability Assessment", or evaluation of corporate sustainability. The criteria are assigned a weight and the general criteria are restricted to less than 50%, similar to the distribution of the remaining balances by sector specifics.

As a suitable instrument for the operationalization of CSR activities of the company we can also use the so-called strategic business performance measurement models that could better illustrate the wide variety of relationships between a company and its stakeholders. These systems are often called "Performance Measurement", and they are defined as a system of measurement using benchmarks from multiple dimensions (cost, time, quality, innovation, customer satisfaction, human resources development) in order to express the performance of various entities in the company (organization units, employees and processes).

The most important systems are the following measurement methods coming form the Balanced Scorecard originally developed by Kaplan and Norton (1992)\textsuperscript{24}. The system goes beyond the financial criteria by including (1) the customer perspective, (2) the perspective of learning and (3) the perspective of internal processes. Despite the effort to balance the appropriate mix of outputs these authors criticize the neglect of certain operational processes. They also highlighting shareholders approach which shows that all causal chain end in the financial perspective without measuring benefits arising from the performance of the company for other stakeholder groups.

Another system is the strategic performance measurement according to the firm Atkinson et al. (1997)\textsuperscript{25}. This seeks to remedy these deficiencies of consistent application of stakeholder management. In their model, the company is seen as the creation of owners, which serves its primary objective - the wealth maximization. The substance of the relationship to other stakeholders is then determined by how they help (or hinder) the achievement of the primary goal. Now the relationships of the various stakeholders derives the so-called secondary targets which are important on their own, but also as a tool to assist the company in achieving the primary goals.
In the Czech Republic the relevant indicators can be found only in the so-called "Standard Responsible Company" Donors Forum, with a specific case of standardization in the field of CSR. This was not assessed (using the LBG methodology Group) for evaluation the effect of specific corporate investments but only for so called Corporate Community Involvement (in particular, CC, philanthropy).

3. THE CZECH SYSTEMS AND THE RATIONALE FOR THE USE OF KORP METHODOLOGY

Standard GRI has been founded in 2000 and it is one of the most widely used standards in reporting. Since October 2006 there was an update of the third directive marked as G3. The purpose of the Directive is to help organizations to create a report as on objective of evaluation of the performance of organization. Guidelines GRI were created initially only for the needs of businesses but later on they began to be used by other organizations and institutions.

One shortcoming of GRI methodology is that the GRI indicators demonstrate only results without proposals to new solution or areas for improvement. These indicators are managerially implemented if they are used in management system of companies. It may not be possible to use the results of measured indicators practically and thus the risk is that the reported results can be at disposal only at particular moment, without further use for the future. Another risk is that the work leads only to passive monitoring, without ambition to manage and improve the relevant processes.

The Czech model (methodology) of evaluation of CSR reporting (KORP) systematically leads the company to check, whether all these areas are adequately addressed.

The practical application of the method

For evaluation of analysis on public firms we use available information in annual financial reports, stand-alone Corporate Responsibility reports and company websites. We use qualitative methodology for measurement of attributes - especially analysis of documents (annual financial reports, ethical rules of firms and others). The analysis concentrates on three pillars – (1) profit, (2) people, (3) planet, so called - Triple bottom line, which divides corporate social responsibility of firms to economic, social and environmental segments.

The profit pillar – economic pillar indicates that the main goal of business is to generate profit, but it must follow certain principles of responsible business. Relationships between enterprises should be based on the principle of win-win that benefits both parties. These principles were described in the Czech literature by Kunz (2012) and they include the following areas: (1) Refusing the use of corruption and unfair competition practices, (2) Transparency and credibility of the company, (3) Relations with stakeholders (customers and suppliers), (4) the behaviour of the owners and shareholders and (5) Compliance with the agreed commercial terms.

The social pillar – is primarily related to the company's employees and to the environment. It is therefore an area of both internal and external nature. Kunz (2012) points out that business owners should be aware of the importance of human capital. According to Kunz satisfied and motivated employee is an important factor for the company success. Caring for staff is currently one of the main issues of corporate social responsibility. There are many activities in this area, and we mention only the most common, which the company can practice (CSR Pillars, 2013) e.g. (1) The employee benefits, (2) Development and training of staff, (3) Corporate Culture, Work-life balance, (4) Human Rights, (5) Equal opportunities, (6) Diversity and employment of persons with disabilities, (7) External Philanthropy and (8) Support of volunteering activities of employees.
The environmental pillar – is associated with environmental protection and tries to reduce the negative impact of production companies on nature. Environmental policy is often readily incorporated into the main corporate strategy. In the area of social responsibility, we can include the following activities according BLF (Business Leaders Forum, 2012): (1) Recycling of waste, (2) Saving energy and water, (3) Restrictions on the use of dangerous chemicals, (4) Protection of natural resources, (4) Production of organic products and services and (5) Reducing Air Pollution.

In our research we use (1–100 points) in every pillar for evaluation of standards according to individual steps of Deming Cycle (PDCA). Every standard has two parts: assumption and result. For evaluation of the KORP method we provide the scoring in the results panel and on assumptions panel. Each sub-criterion can be graded maximum of 100 points and for the weighted sub-criteria stands the same. The formula for calculation is as follows:

\[
\text{Total Points} = \frac{\Sigma BI + \Sigma BII}{\Sigma KrP + \Sigma KrV}
\]

\[\Sigma KrP \ldots \text{The number of ranking criteria in the assumptions panel}\]
\[\Sigma KrV \ldots \text{The number of ranking criteria in the Results panel}\]
\[\Sigma BI = \text{sum of the points of the individual ranking criteria (\Sigma KrP) of the assumptions panel}\]
\[\Sigma BII = \text{sum of the points of the individual ranking criteria (\Sigma KrV) of the results panel}\]

The sample of firms

Target group of firms includes the companies from different profit and non-profit sectors that were using CSR principles during the period of 2011 – 2013. Most of them are owned international investors. This study is intended to assist the Czech firms in their understanding of application of CSR by means of the KORP model based on GRI Framework as a voluntary reporting mechanism. The scope of the present research comprises an investigation of the sustainability reporting of 25 Czech companies (for the preliminary list of companies see appendix 1).

4. SUMMARY AND PRELIMINARY CONCLUSION

In the Czech Republic, the concept of corporate social responsibility is becoming increasingly important. The local pronunciation of CSR trends in the Czech Republic appears to be materialized with some time lag, however, there is an effort on the part of more and more companies to try to engage in social responsibility. It is obvious that the management of companies is aware of the importance of working in all three CSR pillars and assisting the move to sustainable development.

Expected results

In our research we expect to find that companies use correctly the local Czech rating system of corporate social responsibility (KORP). Our findings could help to understand behaviour of the Czech companies in profit or non-profit sector using CSR.

We also expect some controversial issues because of the interpretation of the purpose of CSR that follows logically from the company’s point of view and the angles of interpretation may vary.

We expect to find that the Czech firms prefer to expose themselves in attractive areas of CSR and require immediate and visible effect from the CSR engagement. It is likely that they prefer a quick and simple solution. We expect to find that Czech firms understand CSR as part of their comprehensive marketing approach.

Non-profit companies, however, arise as a marketing tool companies, but with a specific mission, which usually requires long-term solutions of problems that are more complex than keeping in line with the accounting regulations. On the other hand, approach companies forcing NGOs to take care of their performance, to improve the efficiency of its activities, because otherwise they become
the subject of corporate philanthropy. Overall, we can say that CSR is ideally mutually beneficial relationship that ultimately enriches the area in which cooperation between the company and non-profit organizations takes place.

Based on the research, during which we will examine different companies in profit and non-profit sectors and as well as utilizing knowledge from scientific literature and other available sources, we endeavour to characterize the current state of CSR in the Czech Republic. We expect to confirm that CSR is now applied in the Czech companies regardless of their size, which means that it is represented in both large multinational corporations and in small and medium sized businesses. In terms of the business focus of companies that are associated in the Business Leaders Forum, it becomes clear that CSR is applied in companies involved across the broad spectrum of economic activity.

BIBLIOGRAPHY


**APPENDIX 1**

Table 1 Preliminary list of Czech companies in the sample

<table>
<thead>
<tr>
<th>No.</th>
<th>Company Name</th>
<th>Corporate Social Responsibility Report Year</th>
<th>Available Online Date</th>
<th>Available Link</th>
</tr>
</thead>
</table>


---

**ENDNOTES:**

5. [http://kzps.cz](http://kzps.cz)
12. [https://www.globalreporting.org/reporting/G3andG3-1/Pages/default.aspx](https://www.globalreporting.org/reporting/G3andG3-1/Pages/default.aspx)
16. For the preliminary list of companies, please see the APPENDIX 1.
20. [somo.nl/publications-en/Publication_3918/at_download/fullfile](somo.nl/publications-en/Publication_3918/at_download/fullfile)
27. [http://www.lbg-online.net/about-lbg/the-lbg-model.aspx](http://www.lbg-online.net/about-lbg/the-lbg-model.aspx)
TOWARDS TRANSPARENCY IN OTHER FORMS OF FINANCIAL REPORTING – THE ROLE OF IFRS PRACTICE STATEMENT MANAGEMENT COMMENTARY

Joanna KRASODOMSKA
Department of Financial Accounting, Cracow University of Economics
joanna.krasodomska@uek.krakow.pl

Abstract: According to the Preface to International Financial Reporting Standards, other forms of financial reporting include information provided outside of financial statements that assists users in the interpretation of a complete set of financial statements or allows them to make efficient economic decisions. It comprises management commentary which became of interest to the International Accounting Standards Board (IASB) in 2002. The final version of the guidelines for its preparation was released in 2010 as International Financial Reporting Standard (IFRS) Practice Statement Management Commentary. The purpose of the paper is to present the significance of this document for the improvement of corporate reporting transparency. In order to do so, the author analyzed the management commentaries published by two companies from the fuel industry, namely the British BP p.l.c. and the Polish LOTOS S.A., in the years 2009–2013. The analysis aimed at assessing the content and quality of the disclosures before and after IFRS Practice Statement Management Commentary was released. The use of the disclosure index allowed the conclusion that the quality of information disclosed by the companies improved during the research period and in 2013 was higher than in 2009. As expected, the quality of the British company’s disclosures was higher than that of the Polish company. Of all the elements mentioned in the IFRS Practice Statement Management Commentary, the highest quality information was provided on risks related to the companies’ operations. The paper adds to a relatively small number of studies that have dealt with the problem of management commentary disclosures according to IASB guidelines, especially in Central and Eastern Europe.

Keywords: content analysis, disclosure index, IFRS, management commentary

1. INTRODUCTION

The functioning of capital markets is dependent on the information available to their participants. This information should have appropriate quality characteristics and be delivered to users in time for it to be used in decision-making processes. Its desired feature is transparency. The diversity of contexts in which the word “transparency” is used shows how common and, at the same time, imprecise the concept itself is. According to Kothari (2000, p. 91), the term “transparency” is used with reference to corporate reporting interchangeably with the expression “quality of information” so “a precise definition of quality or transparency that everyone agrees on has been elusive.” As Roberts et al. (2005, p. 612) state, “unfortunately it is one of those words that is assumed to have a common basis of understanding, but in fact is used in different ways by different people. Even more unfortunately some omit to explain what they think transparency means’. This view is shared by Barth and Schipper (2008, p. 174). They argue that transparency is not well-defined in a financial reporting context and describe financial reporting transparency as the extent to which financial reports reveal an entity’s underlying economics in a way that is readily understandable by those using the financial reports. The underlying economics are depicted in the statements of financial position, income, and cash flows. According to the authors, they also include information about risks an entity faces and how it manages them. Bushman et al. (2004) define transparency in more general terms as the availability of firm-specific information to those outside the firm.
According to Williams (2005) transparency means: relevant, timely, and reliable information. Zeini (2011, p. 28) writes that the key to enhancing the relevance and transparency of the information disclosed by a company is providing consistent quantitative and narrative reports to accompany financial statements.

Transparency is ensured by various regulations and guidelines forming companies’ information policies. Currently, IASB and its cooperation with FASB has particular importance for the development of information policies of companies operating in Europe. The main aim of the IASB is the issuance of IFRS which contain detailed guidance relating to the general purpose financial statements. However, IASB also mentions “other financial reporting”. The section Scope and authority of International Financial Reporting Standards states that “other financial reporting comprises information provided outside financial statements that assists in the interpretation of a complete set of financial statements or improves users’ ability to make efficient economic decisions” (Preface to International Financial Reporting Standards 2014, par. 7).

A reference to other financial reporting can also be found in the IAS 1. IAS 1 says that “many entities present, outside the financial statements, a financial review by management that describes and explains the main features of the entity’s financial performance and financial position, and the principal uncertainties it faces” (IAS 1, 2014, par. 13). This is particularly important in relation to those activities that are not directly reflected in the financial data or which may be difficult to understand for the user of the financial statements (Helin, 2008). An example of other financial reporting will therefore be management commentary which is the subject of the guidelines released in 2010 in the form of an IFRS Practice Statement Management Commentary. The purpose of the paper is to present the importance of those guidelines for increasing the transparency of corporate disclosures. The remaining part of the paper is structured as follows: the next section reviews the guidelines for the disclosure of information in management commentary in accordance with IFRS Practice Statement Management Commentary. Section three discusses the selected empirical studies devoted to its practical implementation by companies. Section four presents the author’s own research whose aim was to assess the content and quality of the management commentary disclosures of two companies from the fuel industry, British BP p.l.c. and Polish LOTOS S. A., before and after the IFRS Practice Statement Management Commentary was released. The section also provides information on the hypothesis development and research method. It introduces companies under investigation and presents the research results. Section five offers the concluding remarks and indicates the possible areas of further research.

2. IFRS PRACTICE STATEMENT MANAGEMENT COMMENTARY – AN OVERVIEW

According to Aerts et al. (2013, p. 93), management commentary reporting has become an integral part of the accountability mechanisms embedded in the institutional environment of public companies. Like disclosure standards, IFRS Practice Statement is an instrument to keep companies accountable and responsible for past behavior. It is a control mechanism which involves a systematic review of a company’s actions and decisions by stakeholders.

Management commentary became of interest to the IASB in 2002 (table 1). According to its former Chairman, sir D. Tweedie, “management commentary is one of the most useful sections of an annual report, yet many countries applying IFRSs do not have guidelines that cover how to prepare or present this important information. In today’s uncertain financial climate it is particularly important for entities to explain their financial performance relative to their expectations and their strategies” (IASB proposes guidance…, 2009). It should be noted that this

1 Management commentary was mentioned as an example of other forms of financial reports in the Consultative Document concerning the review of the Conceptual Framework for Financial Reporting, other examples included interim financial reports, press releases and supplementary material provided to analysts (A Review of the Conceptual Framework for Financial Reporting, 2013, par. 1.19, p. 17–18).
opinion is not shared by all representatives of accounting profession. Some of them think that the IASB as a standard-setter should deal only with financial statements and focus on accounting standards (Tarca et al., 2010, p. 54).

Tab. 1. History of IFRS Practice Statement Management Commentary development

<table>
<thead>
<tr>
<th>Date</th>
<th>Actions undertaken</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>Project team established (involving Germany, New Zealand, United Kingdom and Canada)</td>
</tr>
<tr>
<td>October 2005</td>
<td>Discussion Paper Management Commentary published by IASB; Comment deadline 28 April 2006</td>
</tr>
<tr>
<td>December 2007</td>
<td>Project moved from research agenda to active agenda</td>
</tr>
<tr>
<td>June 2009</td>
<td>Exposure Draft Management Commentary published by IASB; Comment deadline 1 March 2010</td>
</tr>
<tr>
<td>December 2010</td>
<td>IFRS Practice Statement Management Commentary published by the IASB; Application possible prospectively from 8 December 2010</td>
</tr>
</tbody>
</table>


In the introduction to the IFRS Practice Statement…(2014, IN3) management commentary is defined as “a narrative report that provides a context within which to interpret the financial position, financial performance and cash flows of an entity”. A more extensive definition is presented in the appendix of defined terms (IFRS Practice Statement…, 2014, par. 41). It describes the management commentary as “a narrative report that relates to financial statements that have been prepared in accordance with IFRSs. Management commentary provides users with historical explanations of the amounts presented in the financial statements, specifically the entity’s financial position, financial performance and cash flows. It also provides commentary on an entity’s prospects and other information not presented in the financial statements. Management commentary also serves as a basis for understanding the management’s objectives and its strategies for achieving those objectives.”

The purpose of the management commentary is to provide the users of financial statements with integrated information whose analysis in their context will allow them to obtain a complete picture of the company’s performance. Such information explains the management’s view not only about what has happened, including both positive and negative circumstances, but also why it has happened and what the implications are for the entity’s future. The management commentary should also explain the main trends and factors that are likely to affect the entity’s future performance, position and progress.

The elements of the management commentary and information needs of the users that their presentation is supposed to satisfy, are shown in Table 2.

It is worth noting that although the Practice Statement was developed by the IASB for public companies, it does not mandate which entities should be required to publish management commentary, how frequently an entity should do so or the level of assurance to which management commentary should be subjected (KPMG, 2010). Regardless of the IASB guidelines, individual countries have their own regulations for the preparation of management commentary, which in Poland is called sprawozdanie z działalności (operations report), in the United Kingdom - Strategic Report and in the USA – Management Discussion And Analysis (MD&A). At the European Union’s level, management commentary is regulated by the Accounting Directive 2013/34/EU (Directive 2013/34/EU of the European Parliament and of the Council..., 2013).
Tab. 2. Needs of the primary users of management commentary according to IASB

<table>
<thead>
<tr>
<th>Elements</th>
<th>User needs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nature of the business</td>
<td>The knowledge of the business in which an entity is engaged and the external environment in which it operates.</td>
</tr>
<tr>
<td>Objectives and strategies</td>
<td>To assess the strategies adopted by the entity and the likelihood that those strategies will be successful in meeting the management’s stated objectives.</td>
</tr>
<tr>
<td>Resources, risks and relationships</td>
<td>A basis for determining the resources available to the entity as well as obligations to transfer resources to others; the ability of the entity to generate long-term, sustainable net inflows of resources; and the risks to which those resource-generating activities are exposed, both in the short term and in the long term.</td>
</tr>
<tr>
<td>Results and prospects</td>
<td>The ability to understand whether an entity has delivered results in line with the expectations and, implicitly, how well the management has understood the entity’s market, executed its strategy and managed the entity’s resources, risks and relationships.</td>
</tr>
<tr>
<td>Performance measures and indicators</td>
<td>The ability to focus on the critical performance measures and indicators that the management uses to assess and manage the entity’s performance against stated objectives and strategies.</td>
</tr>
</tbody>
</table>

Source: (IFRS Practice Statement Management commentary 2014, Basis for Conclusions, BC48).

3. PREVIOUS RESEARCH

It can be stated with much confidence that a lot more accounting publications relate to the application of IFRS and financial statements than to other financial reporting, including management commentary. Studies relevant to the author’s own research were conducted by e.g. Mertens and Mieliefste (2011), Ginesti et al. (2013), Carini et al. (2014), Cole (2012) and Girdharry et al. (2011). Their results are briefly presented below.

Mertens and Mieliefste (2011), on behalf of the Netherlands Institute of Chartered Accountants, studied strategic and economic disclosures of 73 largest Dutch publicly listed companies. The conducted analysis revealed that no company incorporated all information items which were included in the authors’ checklist based on the IFRS Practice Statement Management Commentary. However, all companies discussed the nature of their business, including their competitive position (74%), main competitors (22%), environment that influence the entity (95%), product and services (100%) and organization chart (40%). The study also indicates that there is a great diversity of disclosures on strategy reporting. Most of the surveyed companies included a separate strategy paragraph and provided some explanation of how the strategy was to be implemented. However, significantly fewer companies (53%) translated the strategy into performance measures, and even fewer (33%) compared actual outcomes to the long-term strategic objectives. As for performance measures, the authors indicate that financial performance measures were more frequently disclosed, with an average of 3.7 financial performance measures compared to 1.6 nonfinancial measures. Regarding prospective information, almost all the companies provided information on expected future performance. 82% of them included a separate “outlook” section, but only 30% presented targets in that section.

The aim of the research carried out by Ginesti et al. (2013) was to investigate Italian firms’ disclosures in management commentaries in response to the new IASB’s guidance. The authors reviewed the content of the management commentaries published by 66 non-financial firms listed at the end of 2010 on the Italian Stock Exchange. Disclosures were analyzed using a self-constructed checklist based on the guidelines contained in the IFRS Practice Statement. Ginesti et al. found evidence that the general level of disclosure provided by Italian listed firms seems unaffected by IASB’s guidelines. The highest level of compliance with the IFRS Practice Statement was found in the section called the nature of the business, followed by the entity’s principal risks exposures. On the other hand, a lower level of compliance was observed in terms of the disclosure items reported...
in the section called the management’s objectives and its strategies for meeting those objectives and the entity’s structure and how it creates value. The survey also highlights large differences in the level and type of disclosures provided in management commentaries depending on the industry in general or firms in particular.

Italian firms’ management commentaries disclosures were also investigated by Carini et al. (2014). The authors compared the Italian and the United Kingdom companies’ practice in this matter. The analysis was performed for the year 2008 which was the year prior to the publication of the Practice Statement exposure draft. The sample consists of 20 Italian and 20 UK companies. According to the study results, both Italian and UK firms’ management commentaries concentrate mainly on the nature of the business and the description of the results achieved. Strategies, company objectives, and performance measures are presented less extensively.

Another relevant study was done by Cole (2012). Its aim was to assess the general consistency of U.S. companies’ MD&As with the IFRS Practice Statement Management Commentary. 26 nonfinancial companies were analyzed. The research looked only for general consistency of the disclosures with the basic elements of the IASB framework. According to the results, all the companies provided the general information required by the first element of the guidelines, namely, describing the nature of the business. As regards the discussion of company objectives and strategies, 73% of the companies provided a discussion that appeared generally consistent with the element mentioned in the Practice Statement. All surveyed companies provided discussions on resources in the MD&As. As for risk disclosures, the companies included some discussion of uncertainties or risks in MD&As as required by the SEC’s MD&A rules. It is worth mentioning that due to the differences in the US regulations and IFRS Practice Statement, the disclosures made by the companies fail to satisfy the IASB requirements with respect to significant stakeholder relationships. Such relationships can extend beyond related parties and customers (covered by SEC regulations). IFRS Practice Statement also recommends that discussion should include the information on how these relationships affect performance and value and how they are managed. Company prospects were presented by approximately 65% of the sample companies. A discussion of key performance indicators (KPIs) is another component of the IFRS Practice Statement. 81% of the companies were noted to disclose KPIs in some manner. Only approximately 25% of the sample companies provided clear linkage to objectives and strategies for some of their KPIs.

Finally, Girdharry et al. (2011) on behalf of the Certified General Accountants Association of Canada evaluated the selected MD&A sections against the IFRS Practice Statement. The research was based on the review of 124 publicly traded companies. The analysis showed that 83% of the reviewed MD&As were well aligned with the key elements and content structure suggested in the IFRS Practice Statement. Specifically, 27% of the measured companies scored an “average” rating, 45% earned an “above average” rating, and 11% earned an “excellent” rating. A significant number of the reviewed companies responded well to the IFRS Practice Statement guideline to provide an overview of the business and the environment in which an entity operates. However, larger companies tended to discuss quarterly results rather than expand information on the entity’s external environment and the nature of their businesses. MD&As scored well against the IFRS Practice Statement in reporting performance indicators and discussing financial results. An insufficient disclosure of risk factors was observed.

4. RESEARCH METHODOLOGY AND RESULTS

Research aim, hypothesis development and research method
The aim of the study was to determine the content and quality of information disclosed in the management commentaries of two companies, Polish LOTOS and British BP, before and after the IFRS Practice Statement Management Commentary was released. As mentioned earlier, an entity may apply IFRS Practice Statement to management commentary presented prospectively from
December 8, 2010. In view of the above, the research beginning date was the year preceding its introduction, so the research period covered the years 2009–2013.

It was assumed that the mere fact of the IASB interest in the management commentary disclosures would draw companies’ attention to how important this document may be in the communication process with stakeholders and would encourage them to take action in order to improve their disclosures within this section of the annual report. It was expected that the quality of disclosures would improve as companies gained experience in providing them, and in the last year of the analysis the quality would be higher than in the initial year. This allowed the first hypothesis to be formulated:

\[ H1 \text{ The quality of disclosures made by the companies is higher in 2013 in comparison with the year 2009.} \]

The paper evaluated a British company and a Polish company, both from the fuel sector. The United Kingdom is a country in which the Anglo-Saxon model of accounting was established and later adopted by other English speaking countries. It is based on well-developed financial markets and the main source of companies’ funds are shares and other financial instruments. The specificities of the financial system and cultural background in this country resulted in a particularly high range of information disclosed by listed companies. In their annual report, apart from the financial statements, they present additional information relevant for making economic decisions and have a long practice in this matter. In Poland, stock market has operated since 1991, companies finance themselves with the use of bank credits and the companies’ disclosures are mostly regulated by law. However, it should be noted that despite the historical and cultural differences, both countries are members of the EU and their reporting is influenced by the EU Accounting Directive. In view of the above, the second hypothesis is formulated as follows:

\[ H2 \text{ The quality of BP’s disclosures is higher than LOTOS’s.} \]

The authors of the research cited above, Mertens and Meliefste (2011), Ginesti et al. (2013), Carini et al. (2014), Cole (2012) clearly indicate that the companies they analyzed especially widely described the nature of the business. It was assumed that LOTOS and BP would do the same and the third hypothesis was formulated as follows:

\[ H3 \text{ The quality of disclosures concerning the nature of the business is the highest.} \]

In order to determine the quality of information a disclosure index was used. The disclosure index test is a tool consisting of a series of selected items which, after having been ascribed appropriate values, indicate the level of disclosures (Coy 1995 as cited in Guthrie, Abeysekera, 2006, p. 118). The disclosure index may be based on a simple binary system when the aim is to indicate the presence or absence of a given phenomenon. A coding system based on ordinal numbers (usually 1 to 3) can also be used which allows for the variation in the importance of individual factors under analysis. For example, Nicholls (1994), Meek et al. (1995), Vanstraelen et al. (2003), Chavent et al. (2006), Lim et al. (2007), Hossain and Racz (2007), Krasodomska (2008) applied binary index in their research, acknowledging “1” if the information has been observed and “0” in the case of its absence. Authors such as Marston (1986 for Ahmed et al., 2011), Botosan (1997), Robb, et al. (2001) and Nu Nu Htay et al. (2012) used the weighted disclosure index.

In the paper the weighted disclosure index developed by the Girdharry at al. (2011) was used. The authors applied the classification of the management commentary disclosures in accordance with the requirements of the IASB Practice Statement (table 3). A total of 20 detailed items were assigned to eight areas. The quality of disclosures about each element was assessed on a scale of 1–3, where 1 meant “not discussed”, 2 stood for “somewhat discussed”, and 3 stood for “thoroughly discussed”. A “somewhat discussed” score implied that the characteristics were
described in general terms. A “thoroughly discussed” score implied that the characteristics were described in detail and further supplemented with the discussion and analysis identifying possible implications for the company. Overall, a company could receive a maximum score of 60.

Tab. 3. Content elements and their characteristics according to the IFRS Practice Statement

<table>
<thead>
<tr>
<th>Content element</th>
<th>Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nature of the business</td>
<td>- discussion of the industry</td>
</tr>
<tr>
<td></td>
<td>- presentation of the competitive position within the market</td>
</tr>
<tr>
<td></td>
<td>- description of legal &amp; regulatory features that influence the company</td>
</tr>
<tr>
<td></td>
<td>- discussion of the company's main products, services and processes</td>
</tr>
<tr>
<td></td>
<td>- presentation of company structure and economic model</td>
</tr>
<tr>
<td>Objectives and strategies</td>
<td>- description of market trends, threats and opportunities</td>
</tr>
<tr>
<td></td>
<td>- definition of company goals &amp; objectives, providing plans for achievement</td>
</tr>
<tr>
<td>Resources</td>
<td>- identification of major resources used in achieving objectives</td>
</tr>
<tr>
<td>Risks</td>
<td>- identification of principle risk exposures</td>
</tr>
<tr>
<td></td>
<td>- discussion of plans to mitigate risks</td>
</tr>
<tr>
<td>Relationships</td>
<td>- identification of major resources used in achieving objectives (financial &amp; non-</td>
</tr>
<tr>
<td></td>
<td>financial)</td>
</tr>
<tr>
<td></td>
<td>- discussion of how these relationships affect performance (risks &amp; benefits)</td>
</tr>
<tr>
<td>Results</td>
<td>- identification of financial results</td>
</tr>
<tr>
<td></td>
<td>- provision of comparison of results to forecast, previous year and previous</td>
</tr>
<tr>
<td></td>
<td>period results</td>
</tr>
<tr>
<td></td>
<td>- provision of discussion and analysis of any changes in financial condition and</td>
</tr>
<tr>
<td></td>
<td>liquidities</td>
</tr>
<tr>
<td>Prospects</td>
<td>- discussion of future goals and objectives</td>
</tr>
<tr>
<td></td>
<td>- identification of potential risks associated with these objectives</td>
</tr>
<tr>
<td>Performance measures and indicators</td>
<td>- description of indicators that demonstrate company's progress</td>
</tr>
<tr>
<td></td>
<td>- definition of the indicators used</td>
</tr>
<tr>
<td></td>
<td>- discussion of the relevance of indicators used</td>
</tr>
</tbody>
</table>

Source: Girdharry et al. (2011, p. 21)

The following table presents the score range which was used to determine the quality of the disclosures.

Tab. 4. Score range used to determine the quality of disclosures

<table>
<thead>
<tr>
<th>Disclosures quality</th>
<th>Score range</th>
</tr>
</thead>
<tbody>
<tr>
<td>poor</td>
<td>0 – 28</td>
</tr>
<tr>
<td>below average</td>
<td>29 – 39</td>
</tr>
<tr>
<td>average</td>
<td>40 – 45</td>
</tr>
<tr>
<td>above average</td>
<td>46 – 51</td>
</tr>
<tr>
<td>excellent</td>
<td>52 – 60</td>
</tr>
</tbody>
</table>

Source: Girdharry at al. (2011, p. 22)

As in the Girdharry et al. (2011) study, the “excellent” rating was assigned if a company was able to score a “thoroughly discussed” score in at least 80% of the analyzed elements, where the “Poor” rating was assigned if a company scored a “not discussed” score in at least 80% of the analyzed elements.

**Companies under investigation**
The research concentrated on two companies of the fuel industry: BP plc and LOTOS S.A. Both prepare financial statements in accordance with IFRSs.
BP p.l.c. is one of the world's leading international oil and gas companies. The Company provides its customers with fuel for transportation, energy for heat and light, lubricants and the petrochemical products used to make everyday items as diverse as paints, clothes and packaging. The Company operates in two business segments: Exploration and Production, and Refining and Marketing. Its Exploration and Production segment is responsible for its activities in oil and natural gas exploration, field development and production; midstream transportation, storage and processing, and the marketing and trading of natural gas, including liquefied natural gas, together with power and natural gas liquids. Its Refining and Marketing segment is responsible for the refining, manufacturing, marketing, transportation, and supply and trading of crude oil, petroleum, petrochemicals products and related services to wholesale and retail customers. In the years 2009–2012, BP presented Business Review in the annual report, coherent with the EU directive, and Management Report. In 2013, for the first time, BP provided Strategic Report, which replaced Business Review that had been produced before. The regulations require certain new disclosures to be included in the Strategic Report, which were absent in the Business Review, including a description of the company’s strategy and business model (although this was already a requirement under the UK Corporate Governance Code 2012). In June 2014 the FRC issued the best practice statement, Guidance on the Strategic Report, to assist companies in the preparation of their strategic report.

Grupa LOTOS is one of the largest companies in Poland. It is an oil company operating both in Poland and abroad whose business consists in the extraction and processing of crude oil as well as wholesale and retail sale of high-quality petroleum products. The Company produces and markets products such as unleaded gasoline, diesel oil, diesel oil for heating purposes (light fuel oil), aviation fuel and heavy fuel oil. Grupa LOTOS also specialises in the production and sale of lubricant oils and bitumen. Shares of Grupa LOTOS have been listed on the Warsaw Stock Exchange (WSE) since June 2005.

While preparing the management commentary LOTOS followed the basic requirements and guidelines for its preparation contained primarily in the Act on Accounting of 29 September 1994, taking into account the regulations of the EU directives. It should be noted that in Poland works on the release of a National Accounting Standard “Management Commentary” by the Accounting Standards Committee are currently under way. Its project is to a large extent compatible with the IFRS Practice Statement.

Research results
The implemented research method allows an assessment of the quality of the information disclosed in the management commentaries of the surveyed companies. The results are presented in table 5.

<table>
<thead>
<tr>
<th>Company</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>LOTOS</td>
<td>below average</td>
<td>below average</td>
<td>average</td>
<td>average</td>
<td>above average</td>
</tr>
<tr>
<td>BP</td>
<td>average</td>
<td>above average</td>
<td>above average</td>
<td>above average</td>
<td>above average</td>
</tr>
</tbody>
</table>

Source: the author’s own analysis

As can be seen from the data provided in the table, the quality of the information disclosed by the surveyed companies in 2013 was higher than in 2009. The first hypothesis is therefore supported. In subsequent years, the quality of information disclosed by the companies was at least the same as in the previous year or higher. In the case of LOTOS in 2009–2010 it was below average, in 2011–2012 – average, and in 2013 – above average. In the case of BP the change in the information quality occurred only once in 2010 when the assessment “above average” was replaced by “average” and remained at this level until 2013. Excellent disclosure quality was not observed.
The average rate of improvement in the quality of information assessed with the use of the geometric mean was 7% and 2% in the case of LOTOS and BP respectively. Because neither of the companies admitted using the IASB guidelines, it is hard to unambiguously attribute the increase in the quality of disclosures to their implementation. At the turn of 2009/2010 no significant changes in the index values were observed.

The results of the research show the quality of the BP disclosures in the years 2009-2012 to be higher than LOTOS’s, and in the year 2013 to be the same. As can be seen in table 6, the quality of BP’s disclosures concerning most management commentary elements was higher than LOTOS’s, with the exception of the disclosures on risks which were at the same quality level and on results which got a slightly lower score. Despite these differences, the average index value throughout the research period was 41.2 (average) for LOTOS and 47.2 (above average) for BP. This allows the author to conclude that the second hypothesis, according to which the quality of BP’s disclosures is higher, is supported.

For both surveyed companies, the maximum score was awarded to the risks disclosures, and in the case of BP also to the results and performance measures and indicators (table 6). Relationships were found to be the element which got the lowest score in both companies. The disclosures concerning the nature of the business occupied the sixth place in the disclosures quality ranking in both companies. This allows the author to state that the third hypothesis, according to which the quality of disclosures concerning the nature of the business is the highest, is not supported.

Tab. 6. The quality of disclosures concerning the various elements of the MC BP and LOTOS companies in the years 2009–2013

<table>
<thead>
<tr>
<th>Content element</th>
<th>The relation of the score obtained in the evaluation of a given content element to the maximum throughout the whole research period (in %)</th>
<th>LOTOS</th>
<th>BP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nature of the business</td>
<td>63</td>
<td>69</td>
<td></td>
</tr>
<tr>
<td>Objectives and strategies</td>
<td>77</td>
<td>83</td>
<td></td>
</tr>
<tr>
<td>Resources</td>
<td>67</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>Risks</td>
<td>100</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>Relationships</td>
<td>37</td>
<td>50</td>
<td></td>
</tr>
<tr>
<td>Results</td>
<td>93</td>
<td>89</td>
<td></td>
</tr>
<tr>
<td>Prospects</td>
<td>43</td>
<td>47</td>
<td></td>
</tr>
<tr>
<td>Performance measures and indicators</td>
<td>67</td>
<td>100</td>
<td></td>
</tr>
</tbody>
</table>

Source: the author’s own analysis

In addition, the results of the research show that the way information is presented by the two companies improved during the research period. In 2011 BP introduced links between the different parts of management commentary, which significantly facilitated its analysis. In 2010 and 2012, LOTOS changed the way the table of contents was presented which increased the clarity of management commentary. The conducted research also revealed significant differences in the general way information was presented by both companies. In LOTOS it was highly formalized and a strong emphasis was placed on financial data, while BP used more informal language and included a greater amount of non-financial information than LOTOS. In BP’s management commentary the marketing aspect of the disclosed data was also more noticeable.
5. CONCLUSION AND FURTHER RESEARCH

According to Feldman (2010, p. 919), there are two kinds of research relating to the valuation of corporate disclosures in the accounting literature, namely, the numerous works that have examined the information content of financial disclosures and the relatively smaller set of research papers that have studied nonfinancial disclosures, not included in the financial statements and related footnotes.

A particularly important research issue in the case of non-financial disclosures is the transparency of presented data. It makes the data more useful for stakeholders but, at the same time, is largely dependent on the individual decisions of companies since there are no generally accepted standards of making non-financial disclosures similar to those used for financial statements.

According to Tarca et al. (2010), the IASB Management Commentary guidance is timely, and in line with the efforts undertaken to harmonize the accounting standards and reporting requirements on the international level. In the author's own opinion, the fact that IASB published IFRS Practice Statement Management Commentary was of groundbreaking importance. It showed that the issues relevant to the assessment of the financial situation of an entity and the prospects for its future development are addressed not only within the financial statements but also outside it. Management commentary is not a separate annual report section of minor importance which can be used only as a marketing tool for the promotion of the company among investors but an important mean to communicate key information that cannot be included in the financial statements.

According to Arshad et al. (2011, p. 125), “the provision of management commentary in companies’ annual reports is expected to make comparisons of reports more meaningful across borders”. However, differences in non-financial disclosure in management commentary across countries adopting IFRS and other pronouncements issued by IASB are expected to occur due to the firm’s overall institutional setting, including the legal and political system (Soderstrom and Sun, 2007).

In the paper, two companies representing the countries of different legal and political systems were surveyed. One of them was Polish and the other one British. On the one hand, it was expected that the dissimilarities in the accounting systems of the two countries would have an effect on the presentation of information within the companies’ management commentaries. On the other hand, the fact that both countries are members of the European Union justified some expectations of similarities between the information disclosed. It is worth pointing out that the majority of studies referred to in the paper concentrated on companies from one country. The author’s approach was similar to that of Carini et al. (2014) who studied Italian and British companies.

The research results allowed two of the three research hypotheses to be supported. An improvement of the quality of the companies’ disclosures in 2013 in comparison to 2009 and better quality of disclosures in the British company were observed. It should be noted that although the quality of disclosures in the British company was from the beginning at a higher level, the Polish company gradually continued to improve the quality of its disclosures in the following years reducing at the same time the “quality gap” between both companies. Thus the research results did not allow the third hypothesis to be supported. Contrary to the results of the studies conducted by Mertens and Meliefsie (2011), Ginesti et al. (2013), Carini et al. (2014) and Cole (2012), the best quality disclosures were observed with regard to risk and not with regard to the nature of the business.

It should be noted that the research presented in the paper is subjected to certain limitations. Firstly, only two companies were analyzed, which does not allow a broader interpretation of the obtained results. Secondly, the implemented research method, which involves using weighted disclosure index, is to a large extent subjective. Despite the above mentioned limitations, the study contributes to the debate on financial reporting extending the previous literature through an investigation into the disclosures offered by selected firms in their management commentaries. Further research could involve extension of the analysis to a larger number of companies (e.g. non-EU countries, in order to compare the results obtained with those of the firms which do not apply the EU directives), adoption of a longer research period or implementation of a more detailed
classification of the information used in the design of the disclosure index. It would also be interesting to examine whether the compliance with the IASB's guidelines is driven by specific firms' characteristics, such as size or industry. What is more, users' feedback on the usefulness of disclosures made by companies in the management commentary could also be an important and interesting research problem.

Despite the lack of clear information on the application of the IFRS Practice Statement by the investigated companies, substantial comparability of the disclosures with its guidelines can be seen in the case of BP during the whole of the research period and in the case of LOTOS after 2011. In the author's opinion IASB contribution to the increase in the transparency of the disclosures made by the companies should be evaluated positively. The administrative work on the release of National Accounting Standard devoted to Management Commentary disclosures in Poland also deserves appreciation. It seems that another factor which could facilitate future improvement of the disclosures quality in the management commentaries of Polish companies would be greater awareness of accounting students - and future managers - of its importance as part of a company’s information policy. Including information about management commentary in the basic accounting textbooks should also be a good step, as currently it is generally missing.

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IS THERE A LACK OF ECONOMIC THEORY IN ECONOMIC EDUCATION? – A PILOT STUDY IN THE ENGLISH-SPEAKING WORLD AND THE CEE

Dana KUBICKOVA
University of Finance and Administration
dana.kubickova@centrum.cz

Irena JINDRICHOVSKA
Anglo-American University, Prague
irena.jindrichovska@seznam.cz

Abstract: This study deals with the roots and causes of the perceived lack of general education of graduates in economic fields on both sides of the globe - in developed market economies and in economies in transition. We present a pilot comparative study of the contemporary concept of the subject of economics as it is taught to economists, accountants and other professionals at universities in the English-speaking world and in the countries of CEE, particularly the Czech Republic.

Keywords: Economic theory, general education, professional education, training

1. INTRODUCTION AND BACKGROUND

The link between the expectations of academics, practitioners and students about the objectives of accounting education has been much debated. In this paper we want to look into the causes and nature of economic education of accounting professionals. The new trends in education require that the graduates are immediately „usable” in accounting profession. It is therefore ideal that professional training becomes a part of university education. This trend has been followed particularly in the Anglo Saxon tradition and many teaching plans have been influenced by the requirements of accounting associations (McGee, 1998; Coe and Delaney, 2008; Weiss 2011, and Murphy, 2014). This is the way how the university education nowadays linked to professional accounting exams. Universities in the UK incorporated the practice in their teaching plans and one can see a lot of evidence that a particular university XYZ has got 8 out of 9 exemptions from e.g. ACCA examinations if a student studies accountancy at that particular university.

There are four professional associations in the UK in the field of accounting ACCA, CIMA, ICAS and ICEAW. Their orientation slightly differs, but they all provide licences to their members and associates, when their members perform the accounting profession, which is a big attraction for students for their future jobs. And this is also motivating universities and business schools to include the element of examinations in to their curricula. There is also a possibility that a student complies part of professional training whilst studying for his or her degree. This is the resulting in todays’ popular double-degree. In the Czech Republic the accounting and tax education comes from different more continental traditions (e.g. Jindrichovska, Kubickova and Kocmanova, 2014)

2. PREVIOUS LITERATURE

There is a long debate on the relationship of accounting education and professional exams. Business schools want to specialize in topics that are required by professional exams and accounting professors call for more general approach due to recent problems in society induced by globalization, cultural diversity and requirements of knowledge based society.
McGee (1998) in his paper discusses the relation between certification and graduate accounting education from more general perspective namely Law, Economics and Ethics. The article addresses some issues in graduate accounting education from the perspectives of economics, law and ethics. There are separate sections on certification and graduate accounting education, curriculum, faculty and accreditation. The article concludes with some suggestions for a model accounting program.

Authors Coe and Delaney (2008) examine the impact of certifications on accounting education. Certification provides a distinct advantage in the job market and it also signals to employers that a job candidate has the requisite skills needed to perform a specific job. Many accountants find that their degree alone is insufficient for achieving their career goals. Certifications provide students with several opportunities. They allow students to focus on – and demonstrate competency in – specific areas of interest. They also help students identify professional associations and individuals who work in those specialized areas, providing additional opportunities for networking, education, and jobs. Incorporating the learning outcomes related to certifications is a way to ensure that the accounting curricula are providing students with the skills and knowledge they will need in the business world. The authors believe that accounting curricula should consider the content that the certifications have deemed important to practicing professionals. More specifically, accounting educators need to consider whether they are providing students with the tools and expertise that are particularly desirable to employers. Such an approach will help prepare students for the fast-changing business world they will enter.

Sin, Reid and Dahlgren (2011) investigated the issue of work in the accounting profession from the experience of practitioners. The authors claim, that the accounting profession has commercialised its services extensively in the past two to three decades, is facing the challenges of change. An early and concerted response to the changes in the scope of work was the emphasis on developing generic skills in accounting higher education. This study recognises the relevance of accounting practitioners' experiences of the manifestations of change in actual work situations and investigates their conceptions of accounting work. Their research approach identified practitioners' focus of awareness on the functional, outcome and ethical aspects of accounting work. In particular, practitioners described the prevalence of ethics in all facets of their work, their autonomous position and ethical tensions. The pressures of commercialism are also reflected in their conceptions. The findings have raised concerns regarding the adequacy of the present curriculum for preparing accounting graduates for the ethical challenges of work in today's accounting profession. The relevance of developing professional values and identities as a trajectory both within and beyond university learning is advanced.

Authors de Lange and Watty (2011) show that of the various reports released in 2010, two purported to examine the state of accounting education in Australia. These are Accounting Education at a Crossroad in 2010 and Challenges Facing Accounting Education in Australia. Both were released as collaborations of the leading academic organisation, the Accounting and Finance Association of Australia and New Zealand (AFAANZ) or professional accounting bodies in Australia including the Institute of Chartered Accountants in Australia (ICAA), the Institute of Public Accountants (IPA), and Certified Practising Accountants of Australia (CPA Australia). The main thrust of these reports is to examine the challenges facing accounting education in Australian universities and, as such, they act as the input for this AE Briefing. The main challenges articulated in these reports portray a sector suffering from the combined pressure of a large international student enrolment, high student-to-staff ratios, an inadequate funding model, and an ageing academic staff profile. By way of commentary, we suggest that, if these gloomy circumstances continue to develop unabated, then the future for the sector will play out as a 'perfect storm' with the sector suffering on-going troubled development.

Parker, Guthrie and Linacre (2011) explored the relationship between academic accounting research and professional practice. Their editorial offers scope for accounting academics to engage with the profession and society. The paper provides important commentary on the relationship between accounting research and practice as represented in academic journals. The authors claim that research is an important issue in higher education, not only in Australia, but internationally. The paper
acknowledges that accounting academic research is important to the higher education system, careers and publishers. However, its impact on teaching, professional practice, and the professions and society are hotly debated.

According to Weiss (2011) the main cause of changes in the requirements for professional education of accounting is currently the adoption of IFRS on capital markets in Europe and in the USA. That need for education in IFRS caused the need for changes in curricula on universities and college. To better understand how the university accounting programs integrating IFRS into their curriculum, the author surveyed the US universities. According to the survey a significant majority of universities integrated IFRS in years 2009-2011 into their curricula or developed stand-alone courses. The form of implementation varied, but was done even in the universities preparing for local firms, where there was no interest in IFRS.

In their recent paper Boyce, Greer, Blair and Davids (2012) examine a case of accounting education change in the context of increased interest in ethical, social, and environmental accountability. The authors present a reflexive case study of a new university accounting subject incorporating social and critical perspectives. Foundational pedagogical principles and key aspects of curriculum are outlined. The pedagogy draws on the integration of humanistic and formative education (principally based on Gramscian and Freirean approaches) and deep and elaborative learning. Two key aspects of curriculum and pedagogy are analysed. First, a curriculum based on a broad conception of accounting and accountability as power-laden social processes, drawing on a range of research literature. Second, the adoption of an authentic, supportive, and collegial team teaching approach. Students' feedback relating to identified issues is presented. The paper contributes to the renewal of the social and ethical worth of accounting education, concluding that deep accounting educational change encompasses both the content and practice of classroom activity and changes in the self-consciousness of staff and students.

The literature review on the future of accounting has been prepared by Salem (2013) who explains that the second half of twentieth century witnessed, that accounting is an organizer of nearly all business decisions. Accounting is a business where most of the time is spent in face-to-face communications exploring business strategies and positioning. In recent years, accounting education has been under attack and pressure to change its current teaching methods. The Accounting Education Change Commission (AECC) has been a leader in calling for change. They, and others in the accounting profession, have issued statements addressing the structure and objectives of accounting principles courses. These statements have stressed the need for innovative teaching approaches and the importance of incorporating active learning into accounting principles courses. In addition, AECC called to increase the acceptance of international accounting standards and use of computer in accounting education as well as shifting accounting education lecturers' focus from what they teach to what the students learn. This may prepare students to become lifelong learners and keep them aware of the latest developments and enable them to adapt to these developments. This paper aims to uncover suitable criteria for the design and improvement of accounting program and curriculum. More specifically, the goal is to investigate the perilous future of accounting education and discover issues that need to be addressed to improve the learning style and accounting practice.

To conclude, the discussion on the purpose of accounting education is vivid. The purpose of accounting research is being discussed as well as the map of the most suitable accounting degree schemes. The most often discussed topics of recent years are the issues of ethics, sustainability, and implementation of IFRS and new challenges of the globalized business world.

3. THE SAMPLE

In the Czech Republic, there are 72 universities concentrating on different speciality registered with the Ministry of Education of the Czech Republic (public, state and private)\(^1\). Out of this there are

49 universities with economic specialty (in broader or narrower sense). There are 10 universities focused on the preparation for the performance of accounting profession. Seven of them are public universities and two are private universities (see table 1).

Tab. 1. Czech universities and colleges offering degree scheme in accounting to perform accounting profession

<table>
<thead>
<tr>
<th>Name of university</th>
<th>Bachelor degree</th>
<th>Master degree</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Jihočeská univerzita v Českých Budějovicích (JU)</td>
<td>Accountancy and Financial Management of Enterprise</td>
<td>Accountancy and Financial Management of Enterprise</td>
</tr>
<tr>
<td>2 Masarykova univerzita Brno (MU)</td>
<td>Finance and accounting – et present only with specialization Finance</td>
<td>Finance and accounting – et present only with specialization Finance</td>
</tr>
<tr>
<td>3 Mendelova univerzita v Brně (MENDELU)</td>
<td>--</td>
<td>Accounting and taxes</td>
</tr>
<tr>
<td>4 Slezská univerzita v Opavě (SU)</td>
<td>Accounting and taxes</td>
<td>x</td>
</tr>
<tr>
<td>5 Univerzita Tomáše Bati ve Zlíně (UTB Zlín)</td>
<td>Accounting and taxes</td>
<td>--</td>
</tr>
<tr>
<td>6 Vysoká škola báňská-Technická univerzita Ostrava (VŠB-TU Ostrava)</td>
<td>Accounting and taxes</td>
<td>Accounting and taxes</td>
</tr>
<tr>
<td>7 Vysoká škola ekonomická v Praze (VŠE Praha)</td>
<td>Accounting and corporate financial management</td>
<td>Accounting and corporate financial management</td>
</tr>
<tr>
<td>8 Vysoké učení technické v Brně (VUT Brno)</td>
<td>Accounting and taxes</td>
<td>Accounting and financial management</td>
</tr>
<tr>
<td>9 Soukromá vysoká škola ekonomických studií, s.r.o. – Praha</td>
<td>Accounting</td>
<td>--</td>
</tr>
<tr>
<td>10 Soukromá vysoká škola ekonomická Znojmo, s.r.o.</td>
<td>Accountancy and Business Financing</td>
<td>x</td>
</tr>
</tbody>
</table>

Source: www.msmt.cz, own research

The sample under investigation consist of four Czech universities preparing for the accounting profession in their bachelor degree (2) and two out of them both in bachelor and master degree (2) and two professional accounting bodies active in the Czech Republic, that prepare for the accounting profession in special program.

Tab. 2. Universities and Professional associations

<table>
<thead>
<tr>
<th>Universities</th>
<th>Professional associations</th>
</tr>
</thead>
<tbody>
<tr>
<td>3 VSB-TU <a href="http://www.ekf.vsb.cz/cs/">http://www.ekf.vsb.cz/cs/</a></td>
<td></td>
</tr>
<tr>
<td>4 UTB FAME Zlín <a href="http://www.utb.cz/fame">http://www.utb.cz/fame</a></td>
<td></td>
</tr>
</tbody>
</table>

The requirements of professional courses were then compared to teaching plans of four Czech universities that state that they are preparing graduates for accounting profession. In this pilot study we provide comparison in particular with the University of Economics, Prague, Technical University Ostrava, University of Tomas Bata Zlín and Soukromá vysoká škola Znojmo. The first three universities are state universities and the SVSE Znojmo is a private university. It may be worthwhile to broaden our comparison to more Czech universities in particular English speaking universities like UNYP Prague and AAU Prague, but this sample stays limited in this pilot study.
4. METHOD OF ANALYSIS

In our study we use a discursive method to provide comparisons and analysis of sample of Czech universities teaching accounting. We are focusing on one hand on the general subjects like mathematics, economics, ethics, philosophy, languages, statistics and computer science and on the other hand on the specialized subjects like financial accounting, managerial accounting, IFRS, tax, history, financial analysis etc.

In our comparison we expect that there will be lower proportion of general subjects and higher proportion of specialist subjects. The subjects were first classified in two broad categories: General subjects and Specialist subjects and then the degree scheme are assessed in its complexity on the basis of proportion on each group and on the basis of intended goals for students.

It needs to be said at the beginning that the European university education has been traditionally broader than what is a custom in Anglo-Saxon countries where the tradition comes from professional orientation.

5. ANALYSIS

5.1 The Universities

The discursive analysis considers firstly the Czech universities. Furthermore, our analysis allows us to compare different approach to teaching accounting at Czech universities and at professional bodies providing accounting education.

A. VSE – University of Economics in Prague

This university prepares for accounting profession in bachelor degree and master degree in the study specialty Accounting and financial management of enterprise:

In the bachelor's study the student gains the knowledge form the accounting theory from the national and international practices and in financial accounting and reporting and in the cost accounting and manageral accounting, financial analysis and financial management of the business and non-business entities. The study prepares graduates for the performance of functions in financial and manageral accounting (sole entrepreneurs, small businesses, and business companies, non-profit organisations and other bodies), furthermore for the area of internal control, taxes and audits of the financial statements.

The follow-up master's degree prepares graduates for the performance of the methodological and managerial functions in accounting. The study prepares them for the professional function in the area of financial control and auditing of financial statements (audit). Graduates have created professional conditions for the work of the auditor's assistants, accountants and professional audit staff in financial institutions.

B. SVSE Znojmo

This university prepares for accounting profession in this course Accountancy and Business Financing. This course is organized in collaboration with the Institute of Accountants Association Praha, Inc. – the guarantor and the system operator of certification in accounting. Thanks to this cooperation SVSE Znojmo became the only school in the Czech Republic, whose successful students will gain not only a bachelor's degree, but will be able to apply for recognition of most of the relevant examinations to obtain the professional title of "certified accountant". It is based on international educational standards for the accounting profession. Certified Financial ticket is yet to full employment in multinational companies operating in our country, but also throughout the European Union.

The graduate of this programme gains the knowledge from Czech and international financial accounting and reporting, as well as management accounting, financial analysis and financial
management of business and non-business entities. The study also provides insights from the fields of finance, money and capital market, the budget system and tax issues.

The study scheme prepares graduates for positions in financial and management accounting, as well as for the function of internal controls, tax and auditing financial statements.

In general student acquires the necessary knowledge and skills in mathematics, financial mathematics, statistics, basic rights and the use of computer technology to the extent necessary for his professional career. Language education is an integral part of the preparedness of graduates. In the study are required two foreign languages - both in the range of four-semester curriculum.

After completing a bachelor's degree, students have the option of connecting to the Master's program.

C. VSB-TU Ostrava

The goal of the degree scheme Accounting and Taxes at VSB Technical university is to prepare qualified professionals who will be able to perform specialized work and managerial positions in accounting and taxes at the level of middle management.

The graduates of bachelor level can find job opportunities in the field of accounting and tax departments of companies (particularly accounting and tax department of manufacturing and trading enterprises) in non-profit organizations, government organizations, financial institutions, etc. The study contents is focused on the acquisition of knowledge and skills of accounting in manufacturing and non-manufacturing businesses, cost management, costing and pricing, management accounting, taxation and tax administration and related legislation.

The objective of the master's degree in accounting and taxation is to prepare highly qualified specialists who will be able to perform specialized analytical work and management functions related to financial issues at senior and middle management level.

The study is oriented in such a way that the students found their occupation particularly in financial departments and in the financial management of non-financial institutions (manufacturing and commercial enterprises), financial institutions (commercial and investment banks, investment companies, insurance companies) and the economy (state and regional administration). The basis of the study is to gain knowledge in accounting, banking and insurance, preparation of audit activities, international accounting and taxation, financial management and economic analysis.

D. UTB FAME Zlín

The specificity and attractiveness of the degree scheme in accounting and taxes at UTB FAME Zlín University lies in linking academic education with professional training that is focused on the practice of accounting and tax. The subjects learned are firstly the general economic subjects (economics, business administration, computer science and statistics), and subsequently subjects encompassing the subject knowledge of Czech accounting for business and non-business entities, international accounting with an emphasis on the EU, taxation, financial analysis, planning, controlling, and bank legislation.

Graduates will gain a theoretical base to pursue the option of subsequent qualification in the professional examinations to obtain professional certification or to become a tax adviser with final state final examination. The students may then continue in the Master's degree program of Economic Policy and Administration, majoring in Finance at the Faculty of Management and Economics. The main job areas of graduates are positions in accounting and tax, internal audit and finance in manufacturing, business and non-profit organizations in the service sector and institutions of state and local governments

5.2 Professional bodies active in the Czech Republic

Subsequently, after analysing universities we concentrate on professional accounting bodies that perform their activity in the Czech Republic. There are two active associations: Union of Accountants
(Svaz účetních) which provides certification since 1999 and the ACCA Association of Chartered Certified Accountants (ACCA Czech Republic, Slovakia and Hungary) that operates in the Czech Republic since 2003.

A. The Union of Accountants
The Union of Accountants in the Czech Republic has been founded in 1990 as the successor of the Association of Accountants and statisticians, who worked (however not as an independent body) since 1969. This change was supposed to recognize the change in the economic environment and develop the fundamental basis of a suitable model in new economy. The performed research amongst the Union members has shown that some aspects of the existing system certifications can be viewed as a motivating little or too complicated.

Subsequently a team under the supervision of the Association of Accountants experts appointed by the European Commission in Brussels and in close cooperation ACCA has suggested a suitable model for reflecting the transformation of the Czech economic environment. The project was supported by Phare funds, result of which was implementation of the education and certification of accountants. Since the year 1999 the certification was a three-stage procedure (accounting assistant, financial statement accountant and accounting expert). There was a major change in the certification structure in 2007 to accommodate the new requirements of accounting education. Subsequently there is a new structure of exams since September 2008 and qualification can be acquired in two levels: certificated accountant (CCA) and accountant expert (CPA).

The style of exams has changed, because it was perceived as too academic and the whole scheme was perceived as a relatively demanding high school, without official accreditation of the Ministry of Education and without an academic degree.

Nevertheless, the original intention of this qualification was to develop a system of professional training combined with practice is not intended to substitute for higher education. The main goal of this professional specialization was acquisition and consolidation of practical procedures and methods used in accounting practice. Acquiring theoretical knowledge practically applied to specific instructions and procedures. This change, therefore, lead to greater compatibility with the ACCA New Syllabus and modern conception and included some new disciplines that gained new importance.

B. The ACCA
The Association of Chartered Certified Accountants is the global body for professional accountants with aim to offer business-relevant, first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management. It provides services through a network of 91 offices around the World. In the Czech Republic ACCA operates for the regions Bohemia, Slovakia and Hungary since 2003.

The ACCA exams are divided into two levels; Fundamentals and Professional. The Fundamentals level encompasses two modules Knowledge and Skills. The Knowledge module introduces the main areas of financial and management accounting. In the Skills module there are six subjects covering the main technical areas that accountants are expected to know.

The Professional level is divided into two modules: Essentials and Options. Both of the modules at Professional level have been set at the same ability level as a university Master’s degree. This level builds on the technical knowledge gained in the previous level and it encompasses more advanced professional skills, techniques and values. These are required at a senior level by accountants working in an advisory or consultancy role. Students have to pass the three papers in the Essentials module and two out of four Options papers.

It seems that the ACCA examinations and the degree structure is more divorced from university education and concentrates on specialist subjects that are readily usable in professional accounting.
6. RESULTS

By comparing the professional exams and Czech educators we see that some universities come very close to requirements of international professional bodies. We expected to find minor role of local accounting practices and major role of international practices in particular with regards to IFRS. We expect to find national regulation with respect to taxation.

Tab. 3. Comparison of teaching plans at Czech universities teaching accounting and plans of Professional associations

<table>
<thead>
<tr>
<th></th>
<th>UE (VSE) Prague</th>
<th>PCE (SVSE) Znojmo</th>
<th>VSB-TU Ostrava</th>
<th>UTB Zlin</th>
<th>Certification of accountants (CzAA)</th>
<th>ACCA</th>
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<tr>
<td></td>
<td>Abs. %</td>
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<tr>
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<td>22</td>
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<tr>
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<tr>
<td>Compulsory optional</td>
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Note: G = general, S = specific

A comparison of curricula of bachelor's degree can be summarized that the prevailing share has generally focused subjects in three of the four universities. VSE Praha has a slightly lower proportion of general subjects. To the contrary as it could be expected the professional training program at both institutions (ACCA, AA CR) shows predominance of specific disciplines.

From the universities compared the highest proportion of wide-ranging general subjects displays the UTB Zlin, whilst the lowest proportion is at the University of Economics in Prague. As it concerns the curricula of master's degree at the two universities, the situation is balanced: one has a larger share of general subjects and the other has a greater proportion of specialties. Professional preparation ensures in both cases a higher degree of grounding in specific subjects. In the case of AA CR it is 100%.

For comparison with the Czech universities we have chosen a British flagship – the London School of Economics. At the London School of Economics the degree programme in Accounting and Finance is concerned with more than just computational skills. Both subjects Accounting and Finance
are central to the way in which management, shareholders and various other stakeholders understand and seek to change and control the nature of organisations, as well as to how the market allocates finance to firms.

The university prepares graduates to work in the areas of professional accountancy, investment banking, investment analysis, management consultancy and financial management, as well as further academic study.

The bachelor degree involves studying 12 courses over three years, plus LSE100 (compulsory course at the beginning of study). Half of the courses are in accounting and finance, and half in related disciplines. The students have an opportunity to specialise in various fields within the subject area. The graduate degrees involve studying 6 compulsory courses and four compulsory optional courses from the range of 20 optional courses of both general and specific nature.

7. CONCLUSION

To the contrary to our initial expectations, we have found that at Czech universities general subjects are not neglected. Students spend more time learning general subjects in their bachelor studies and subsequently they concentrate on more specialist subjects in their master’s studies.

Professional education is offered by two main associations that function in the Czech Republic the ACCA and the Czech Accounting Association (CzAA). The professional association concentrates mainly on specials subjects but on its own include general subjects mainly in law and ethics. The reason for the concentration on ethics must be the pressure on eliminating accounting scandals after 2002 (Sarbanes Oxley Act).

We expect to find that cultural differences and traditions do not play so big role in today’s university education. Rather, there is the orientation on professional practicing accounting and practical financial management. However contradictory trend as occurred recently, where many universities offer so called double degree. This trend has surprisingly penetrated also to the accounting education, when the ACCA now offers double degree with Oxford Brookes University. So it seems that accountants perceive that they need broader educational basis, not just specialist accounting subjects. Furthermore tis led to greater recognition of accounting education aspiring to gain university level.

8. LIMITATIONS OF THE STUDY

This study provides a picture on the proportion of general and specialist subjects at Czech universities. So far in this study we did not explore other indicator than number of general and specific subjects. We could also explore the number of credits that are associated with each subject to increase the explanatory power of the study. Another view on the problem might be to explore the nature of electives that were actually chosen by students. Another way would be to explore the degree schemes of universities and compare and assess qualitatively the learning outcomes. Also the classification of courses to general and specialist requires a more detailed justification (i.e. classification of the course financial mathematics or information technology etc.)

We are also aware that the sample of Czech universities under investigation is rather limited. On the other hand this sample encompasses all Czech universities that are explicitly claiming that they prepare students for the career of professional accountant. Methodologically, she study could explore the possibilities of content analysis and also more precisely define and assess the terms of general and specific knowledge.

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2 The course LSE 100 introduces students to the fundamental elements of thinking like a social scientist. LSE100 uses current issues of public concern and intellectual debate to explore these questions from the perspective of different disciplines.

3 London School of Economics – Degree Programme characteristics. Available at: http://www.lse.ac.uk/study/undergraduate/degreeProgrammes2015/accountingAndFinance/NN34_BSc_accfin.aspx, online [08-18-2014].

ACKNOWLEDGEMENTS
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- [http://www.utb.cz/fame](http://www.utb.cz/fame)
- [http://www.svse.cz/studium-studijni_obory_studijnih_programu_ekonomika_a_management-ucetnictvi_a_financni_rizeni_podniku](http://www.svse.cz/studium-studijni_obory_studijnih_programu_ekonomika_a_management-ucetnictvi_a_financni_rizeni_podniku)
ACCOUNTING CONSERVATISM IN EUROPE: A LITERATURE REVIEW

Ema MAŞCA, Ramona NEAG
Petru Maior University of Tîrgu Mureş, Romania
ema.masca@ea.upm.ro

Abstract: The aim of this study is to present a literature review for accounting conservatism. Initially theoretical background is examined for accounting conservatism which consists of definition and explanations for existence of accounting conservatism to provide a better insight. Then academic studies on accounting conservatism are analyzed under two major categories. Due to the vast number of studies, the latest and most commonly cited ones in well-known academic journal or meetings are selected to be presented. In our research we aimed in particular the impact of IFRS adoption on accounting conservatism in Europe. Recent exemption of conservatism (prudence) from IASB’s Framework enhances the significance of the topics as a research question. Our study shows that following the adoption of IFRS, the level of conservatism decreased in countries whose local GAAP was closer to IFRS, but that now, big companies manifest a need of conservatism.

Keywords: accounting conservatism, Europe, IFRS adoption, literature review

1. INTRODUCTION

Accounting conservatism is one of the oldest concepts in accounting. Even if the debates on accounting conservatism are as old as its existence, latterly, IFRS adoption in the countries of Europe, led to emphasizing discussions on this concept. Currently, the International Accounting Standards Board believes that conservatism should not be named in Conceptual Framework for Financial Reporting, but in the International Financial Reporting Standards (IFRS) there are presented more conservative techniques. Promoting or not the accounting conservatism by IASB depends on the influence that accounting conservatism has on the quality of financial reporting. In this study we try to provide a literature review on the impact of IFRS adoption on accounting conservatism. Our study shows that following the adoption of IFRS, the level of conservatism decreased in countries whose local GAAP was closer to IFRS, but that now, big companies manifest a demand for conservatism.

In the second part we present definitions of accounting conservatism and clarifications of this concept. In the third part, we present twelve papers that studied the impact of IFRS adoption on accounting conservatism as a dimension of the quality of financial reporting. The last part presents the findings and conclusions of this study.

2. THE DEFINITION OF ACCOUNTING CONSERVATISM

Accounting conservatism is a financial approach many companies use to limit the amount of risk in their accounting information. Companies may use this approach to avoid misleading internal or external business stakeholders regarding the company's financial health.

Sudipta Basu (1997) interpreted conservatism as capturing accountants’ tendency to require a higher degree of verification for recognizing good news than bad news in financial statements (earnings conservatism). Under his interpretation of conservatism, earnings reflect bad news more quickly than good news. For instance, unrealized losses are typically recognized earlier than
unrealized gains. This asymmetry in recognition leads to systematic differences between bad news and good news periods in the timeliness and persistence of earnings (Basu 1997).

Gerald Feltham and James Ohlson (1995), approached conservatism from the view of understatement of the book value of shareholders’ equity (balance sheet conservatism). The long term result of accounting conservatism is an understatement of net assets. When comparing two accounting treatments, the treatment that generates a lower value of net assets will be classified as more conservative, and vice versa (Hellman, 2008). Juan Manual García Lara and Araceli Mora (2004) demonstrated that in United Kingdom, Germany, France, Switzerland, the Netherlands, Italy, Spain and Belgium there are both balance sheet and earnings conservatism practices. In addition, they found that the existence of balance sheet conservative practices is associated with reduced levels of earnings conservatism.

The idea of systematically understating assets and overstating liabilities, recognizing revenues too late and expenses too early has been interpreted by critics from the Anglo-American tradition as the way of reducing the relevance of accounting information. Conservatism is, at its best, a very poor method of treating the existence of uncertainty in valuation and income. At its worst, it results in a complete distortion of accounting data (Niclas Hellman, 2008, citing Hendriksen, 1982).

Ross Watts (2003a) shows that conservatism may be defined as the minimal differential verifiability required to recognize profits versus losses. Watts stated that conservatism is the asymmetrical verification requirement for gains and losses.

The focal point in conservatism is dividend policy, and there is no evidence that use of the ‘cost-or-market’ is an effective means of insuring proper care and caution, year by year, in the declaration of dividends. This need not be surprising when it is recalled that the amount by which income is understated in one year through the application of ‘cost-or-market’, as compared to the use of cost, is in effect added to the showing of income in the following period. (Hellman, 2008, citing Paton and Littleton, 1940, p. 128).

Dan Givoly, Carla K Hayn și Ashok Natarajan (2007), measured reporting conservatism. The systematic understatement of net assets is a result of conservative accounting treatments; the understatement of net assets is determinated by financial reporting system that fails to capture positive present value projects and subsequent increases in the value of assets. Historical cost convention coupled with the transaction-based accounting approach and the assumptions of going concern and a stable monetary unit are the examples of financial reporting features that cause this kind of conservatism. Management has limited or no discretion in deviating from this type of conservatism (Gokmen, 2013). The other two sources of conservatism are minimization of assets on the balance sheet (the lowest value includes lower of cost or market accounting for inventory and impairment accounting for long-lived tangible and intangible assets) and the recognition of losses in a more timely fashion than gains. In these latter kinds of conservative management has discretion to affect the level of conservatism that is applied while preparing financial statements.

Conservatism has influenced accounting practice and theory for centuries.

If accounting were not regulated, contracting parties would voluntarily agree that the accounting numbers used to partition cash flows amongst them should be determined conservatively (Basu, 1997).

For management, that conservatism is essential. Managers will bias and noise value estimates, because there is a lack of verifiability, managers have limited tenures and limited liability. The emergence of the conservatism principle and the preparation of audited financial statements can be ascribed to managerial attempts to bond against exploiting their asymmetrically informed position relative to other claimholders. Debtholders and other creditors also demand timely information about ‘bad news’ because the option value of their claims is more sensitive to a decline than to an increase in firm value.

There exist different types of prudence or conservatism distinguished in the academic literature. The value of conditional conservatism (news driven, ex post conservatism), which provides unfavourable news in a more timely fashion than good news, has drawn much attention in
The value of unconditional conservatism (news unrelated, *ex ante* conservatism), which measures assets at a lower amount than their actual value and is mostly driven by regulation, is still a matter of research (Gebhardt, Mora, Wagenhofer, 2014). Conditional conservatism is distinct from unconditional conservatism, which involves the predetermined understatement of the book value of net assets, as occurs with the immediate expensing of the costs of most intangibles.

Under unconditional conservatism, the book value of net assets is understated due to predetermined aspects of the accounting process. Under conditional conservatism, book value is written down under sufficiently adverse circumstances, but not up under favorable circumstances. However, sometimes the conditional conservatism could have adverse consequences (e.g., induces managerial risk aversion) and/or unconditional conservatism could have favorable consequences (e.g., alleviates material risk aversion).

Some authors (Beaver and Ryan, 2005) show that conditional and unconditional conservatism are interrelated, in particular, unconditional conservatism creates accounting slack that preempts conditional conservatism, and so it is inherently limited to consider conditional conservatism separately from unconditional conservatism.

Other authors (Iatridis, 2011) consider that conditional form of conservatism is negatively related to unconditional conservatism, as the former tends to enhance contracting efficiency, while the latter might facilitate managerial opportunism.

Examples of unconditional conservatism include immediate expensing of the cost of internally generated intangible assets and amortization of long-lived assets at a rate above the expected economic amortization rate. Beaver and Ryan (2005) discuss, there is a complex interplay between unconditional conservatism, past applications of conditional conservatism, and future applications of conditional conservatism that remains to be fully explored.

Previous literature suggests many alternative explanations for conservatism in financial reporting. Watts (2003a), Ball și Shivakumar (2005), Basu (2005) and other au identified four main triggering factors for conservatism: contracting, litigation, taxation and regulation. While contracting considerations appear to explain the origins of conservatism, tax, litigation, political process and regulatory forces have also influenced the degree of conservatism.

George Gotti (2008) shows that the first explanation is its use as efficient technology employed in firm governance. A conservative accounting approach is used to deal with the moral hazard determined by the asymmetric information, limited liability, and asymmetric payoffs of the different parties involved in the firms, e.g. management compensation and debt contracts. The second possible explanation for accounting conservatism is limiting shareholders’ litigation. Overstating a firm’s net assets is more likely to increase the litigation costs for the firm than understating net assets. Thus, with conservatism, the firm reduces its expected litigation costs. The third possible explanation is taxation; in profitable firms, conservatism reduces the present value of taxes, thus increasing the value of the firm. The fourth possible explanation of conservatism in financial reporting is standard setters’ and regulators’ incentives. Both standard setters and regulators are exposed to asymmetric loss functions because they would be more criticized if they adopt accounting standards that favor overstatement of net assets instead of understatement of net assets. Finally, the fifth reason for conservatism in financial accounting is that conditional conservatism may serve as a corporate governance mechanism to reduce the information asymmetry among the various parties (managers, shareholders, investors, stakeholders in general) involved in firms’ contracts, litigation, taxation, and regulation processes. Much of the information asymmetry arises from the firm’s investment opportunity sets, but it also occurs because the firm’s management, more informed about events and investment opportunities, formally collects and reports information to stakeholders.

Ross L. Watts (2003b) elaborates several measurements for conservatism, draws evidences on alternative conservatism explanations and on non-conservatism explanations. The writer concludes that existing evidence for accounting conservatism is most consistent with the contracting and litigation explanations.
Xinrong Qiang (2007) found that contracting induces conditional conservatism; litigation induces both forms; regulation induces unconditional conservatism; and taxation induces unconditional conservatism. These findings indicate that the two forms of conservatism play distinct roles in contracting, regulation, and taxation, as well as a common role in litigation. They also play an interrelated role, as suggested by the finding that unconditional conservatism reduces conditional conservatism. The combined evidence implies that because the two forms meet distinct needs but are negatively interrelated, it is necessary to trade them off.

Gunther Gebhardt, Araceli Mora and Alfred Wagenhofer (2014), show that existing research suggests that conditional conservatism is important in debt contracting. Empirical and analytical research shows that conservatism is valuable because it facilitates the monitoring of debt contracts and reduces the cost of debt, facilitates the access to additional debt funds, and reduces risk shifting and shareholder–bondholder conflicts over dividends.

Though they consider that contracting and litigation induce conditional conservatism, and taxation and regulation probably produce just conservatism in its unconditional form, Juan Manuel Garcia Lara, Beatriz Garcia Osma and Fernando Penalva (2009), find that taxation and regulation induce not only unconditional conservatism, but conditional conservatism as well. As regards contracting, they believe that its complexity can constitute an interesting ground for future research.

Previously, IASB defined conservatism as follows: “…Prudence is the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities and expenses are not understated. However, the exercise of prudence does not allow, for example, the creation of hidden reserves or excessive provisions, the deliberate understatement of assets and income or the deliberate overstatement of liabilities or expenses because the financial statements would not be neutral and therefore not have the quality of reliability.” (IASB Framework for Preparation and Presentation of Financial Statements, 2001, paragraph 37).

Actually the situation explained above was available until recently. Because conservatism is excluded from IASB (International Accounting Standards Board) Conceptual Framework for Preparation and Presentation of Financial Statements, as 2010, as a result of joint project between IASB and FASB (Financial Accounting Standards Board).

George Gotti (2008), atrage atenția asupra faptului că în 2006, the US Financial Accounting Standard Board (FASB), jointly with the International Accounting Standard Board (IASB), stated: Neutrality is incompatible with conservatism, which implies a bias in financial reporting information. […] Conservative or otherwise biased financial reporting information is equally unacceptable. Now, IASB considers that fundamental qualitative characteristics of useful financial information, are relevance and faithful representation. And by increasingly broad adoption of IFRS globally they find that companies move their interest from the conservative accounting to fair value accounting (Lu and Trabelsi, 2013).

While the IASB argues that the reason for omitting the concept is related to trying to be unambiguous and to avoid misinterpretations, others argue for the need to explicitly reintroduce the concept of prudence in the Conceptual Framework (Gebhardt, Mora and Wagenhofer, 2014).

Paul Andre and Andrei Filip (2012) show that IFRS are more principle based than rule based. Examples of IFRS neutrality include greater use of fair values, impairment testing rather than amortization including the possibility to reverse prior impairments and clearer rules on how and when to book provisions. Although, IFRS present numerous mechanisms to manifest conservatism. Richard Macve (2014) citing (Lambert, 2010) suggest that the relevant issue is not so much “fair value versus conservatism” but rather “how much conservatism for different purposes and situations?”

Although the boards suggest that the improved framework will not include prudence or conservatism as desirable qualities, a more valid description is that consistently conservative accounting treatments will be replaced by accounting methods that leave more opportunities for temporary conservatism. Niclas Hellman (2008), speaks about changes in accounting estimates that temporarily understate net assets via the creation of hidden reserves which later may be reversed.
From user’s perspective, temporary conservatism is demanded because of the increased income-shifting between periods. The mixing of consistent and temporary conservatism may lead to counter-intuitive interpretations of the underlying business activities that, in turn, make the information less relevant to users.

3. EMPIRICAL STUDIES ON THE IMPACT OF IFRS ADOPTION ON ACCOUNTING CONSERVATISM IN EUROPE

In this section there are analyzed twelve studies on the impact of IFRS adoption on accounting conservatism in Europe. We shall present the evolution of accounting conservatism on different levels that have already been studied. We'll have thus a picture of the effects of IFRS adoption in Europe and also of the demand for conservatism of the companies, investors, potential investors and other users of financial information.

1. Paul André, Andrei Filip, (2012), Accounting Conservatism in Europe and the Impact of Mandatory IFRS Adoption: Do country, institutional and legal differences survive?
   
   Objective: Paul Andre and Andrei Filip examined the impact of the mandatory change to IFRS in 2005 by European firms on the level of accounting conservatism and check whether well documented differences in conservatism across countries and varied institutional and legal settings survive the change.

   Sample: Their sample consists of 2,477 mandatory IFRS adopters from 16 European countries.

   Model(s): They use the empirical approach first suggested by Basu (1997).

   Finding: They found that conservatism has also decreased across code law countries; French and German law origin countries; countries with higher perceived levels of governance, shareholder protection and enforcement; and countries with important debt markets and with less developed equity markets. More specifically, the level of conservatism decreased in France, Germany, Greece, Netherlands, Portugal, Spain and Switzerland. They found also that countries for whom IFRS meant the greatest difference in both accounting standards and extra disclosure, experience a reduction in conditional conservatism. Finally, countries where the tax book conformity was high, also experience a significant reduction in timely loss recognition.

   More importantly, they document that differences across countries, institutional and legal settings disappear after mandatory IFRS adoption. The level of conservatism post-IFRS is not significantly different across the vast majority of EU countries (with the exception of Italy and Switzerland, being less conservative), across legal origins or traditions, across governance, investor protection, and public enforcement regimes, across debt-based or equity-based economies or across more different tax-book conformity regimes.

   They found just weak evidence that insider economies with weak enforcement continue to have a lower level of conservatism. Finally, the decrease in conservatism is most significant in countries which had the greatest difference with the new IFRS standards.

   So, whereas legal incentives, financial systems and accounting traditions prior to IFRS lead to varying levels of conservatism, the mandatory IFRS adoption has reduced conservatism and all the more, the differences in the level of conditional conservatism across European listed firms.


   Objective: They study the effect of the mandatory adoption of IFRS in Europe in 2005 on conditional conservatism.

   Sample: Their sample consists of 7,251 firm-year observations drawn from 16 European countries.
Model(s): They use three measures: the Basu (1997) measure, the Khan and Watts (2009) measure, and a measure controlling for potential shifts in unconditional conservatism and cost of capital after the adoption of IFRS.

Finding: They document a decrease of the conditional conservatism after the adoption of IFRS, even though IFRS have reduced the level of unconditional conservatism, and put in place mechanisms to ensure conditional conservatism such as impairment testing. They find that the decrease of conditional conservatism has occurred in strong enforcement/governance countries, with no change in the converse. They show that the decrease of the conditional conservatism is greatest in firms having high levels of intangibles; therefore, that inappropriate impairment testing is a potential explanation. The implementation of impairment tests (in particular for intangibles with indefinite useful life) usually relies on valuation models, requires ‘significant judgment’ from managers, and is prone to manipulation by managers because it relies on unverifiable fair value estimates. Their results inform standard-setting stakeholders about a potential negative effect of the greater flexibility permitted by IFRS on a key dimension of accounting quality. They are important for European regulators and standard setters as they review the cost and benefits of IFRS.


Objective: Qi Chen, Thomas Hemmer and Yun Zhang studied the role of conservative accounting standards in alleviating rational yet dysfunctional unobservable earnings manipulation.

Model(s): They use an analytical model with endogenous demand for financial reports.

Finding: When accounting information serves dual purposes (i.e., valuation and stewardship purposes), their model shows that the current owner of a firm has an incentive to engage in earnings manipulation activities in hope of boosting the market price of his firm. However, potential investors rationally expect and price protect against the earnings manipulation. Lacking the tools for not to manage earnings, the current owner is trapped by such expectations and therefore has to manage earnings in order to fulfill potential investors’ rational conjecture. As a result, inefficient earnings manipulation exists, adding not just bias but also noise to the performance measure used to motivate the firm’s employees.

Their analysis also shows that employing conservative accounting standards can actually reduce the equilibrium amount of both noise and bias and thus help achieve a more efficient equilibrium outcome. This occurs despite the fact that conservative accounting itself introduces undesirable biases/noises and that the current owner maintains all manipulation options. As shown, the reason it works is that adding some known (stochastic) conservative bias reduces the impact of news on share prices and consequently reduces the benefits of earnings management, given potential investors’ belief.

4. Niclas Hellman, (2008), Accounting Conservatism under IFRS

Objective: Niclas Hellman analyzed how the conservatism principle is applied under IFRS. This was done via an analytical examination of three cases relating to three different IFRSs: (i) judgement related to the recognition of deferred tax receivables pertaining to loss carryforwards (IAS 12); (ii) judgment regarding the capitalisation and impairment of development costs (IAS 38); (iii) judgment regarding the use of the percentage-of-completion method and the zero-profit recognition method during the completion of construction contracts (IAS 11).

Model(s): Three cases are related to three different IFRSs (IAS 12, IAS 38 and IAS 11, respectively). Each case is analysed by using a numerical example and illustrated by using an annual report example

Finding: In essence, the analytical examination of the three standards suggests that IFRS reduces the consistent conservatism (consistent understatement of net assets) that was a prevalent feature of prior accounting treatments; at the same time, however, IFRS leaves more opportunities for temporary conservatism, i.e. changes in accounting estimates that temporarily understate net assets, via creation of hidden reserves, which later may be reversed. From a user perspective,
temporary conservatism can be viewed as demanding because of the increased income-shifting between periods.

Also, Niclas Hellman evaluated the user implications of mixing accounting treatments with varying degrees of conservatism. He considers, for example, the treatment of R&D expenditure. A consistently conservative treatment of such expenditure is to expense all of it immediately when incurred. The application of IAS 38 may lead to some part of this R&D expenditure being expensed and some part being capitalised, depending on the preparer’s estimates and probability judgments. This implies that the financial statements will reflect a mix of R&D expenditure that is immediately expensed (consistent conservatism) and R&D expenditure that is capitalised and subsequently impaired or amortized, leaving opportunities for temporary conservatism. In sum, the results suggest that the mixing of consistent and temporary conservatism may cause counter-intuitive interpretations of the underlying business activities that, in turn, make the information less relevant to users. The empirical examples indicate that there are behavioural reasons from a management control perspective to choose a consistently conservative treatment in the internal accounts.

5. Cristy Lu, Samir Trabelsi, (2013) Information Asymmetry and Accounting Conservatism under IFRS Adoption

Objective: This study investigates how accounting conservatism changes after mandatory IFRS adoption.

Sample: They focus on a sample of European countries which required mandatory adoption of IFRS after 2005. The final sample includes 1,954 firms from 19 countries.

Model(s): They use the empirical approach first suggested by Lafont and Watts (2008).

Finding: The empirical findings of this study shows that the level of accounting conservatism decreases after mandatory IFRS adoption and reached the lowest point before 2008. However, in 2008, accounting conservatism sharply increased, likely due to the global economic crisis. This supports the idea that the enhancement of accounting conservatism is an efficient mechanism to increase information credibility, even though investors expect higher reporting quality after mandatory IFRS adoption.

Moreover, this study shows that information asymmetry is positively related to accounting conservatism, consistent with LaFond and Watts (2008), and the adoption of IFRS will weaken the relationship between them. People would turn to other information sources after the adoption of IFRS which is an allegedly principle-based accounting standard. This might be because IFRS lowers the level of accounting conservatism and, therefore, lower the credibility of accounting, threatening the role of accounting as an information source. Consequently, it is better to maintain accounting conservatism to some level instead of blindly lowering it.

Finally, this study shows that conservative accounting increases information environment by providing comparatively credible information, because there is a significant positive relationship between conservatism and analysts following.


Objective: In their study, Hanna Embring and Johan Wall (2012), aimed to establish what effect the 2005 IFRS adoption has had on accounting conservatism in Sweden.

Sample: The study uses observations from 430 companies listed on the Swedish stock exchanges.

Model(s): The regression analysis model selected for measuring conservatism, was developed by Sudipta Basu in 1997.

Finding: The findings of the study indicate that since the IFRS adoption, conservatism has decreased among listed Swedish companies. They have furthermore found evidence that although conservatism has decreased, it has not completely disappeared from accounting practices.
This study does not explain the causes behind the decreasing conservatism in Sweden. We see that conservatism has indeed decreased after the adoption, but if it is as an effect of the IASB’s stance on conservatism or of a general movement in society is difficult to say. The findings of this study, that conservatism has indeed decreased in Sweden in the period after the 2005 IFRS adoption, has implications not only for the professional accountants and auditors but also for investors and other users of financial statements. Considering that the IASB is striving towards limiting the practice of conservative accounting due to what they regard as negative bias and threat towards neutrality, decreasing options for conservative practices may be facing all countries that use IFRS. The changing reporting trends noted in this study may therefore affect an even wider group of people than just the ones engaged in the Swedish market. Regardless, it is the options of IFRS that enables this to be expressed to a greater extent than the more limiting previous Swedish GAAP.

7. Samira Demaria, Dominique Dufour, (2007), First time adoption of IFRS, Fair value option, Conservatism: Evidences from French listed companies

Objective: The paper studies the first adoption of IFRS within the perspective of the accounting options concerning the fair value method. The optional standards included in the study are: fair value exemption of IFRS 1, IAS 16, 38 and 40. The paper pursues two main objectives. Firstly, from an explanatory point of view, French fair value choices during the first adoption of the IFRS are presented. The second goal of the article is to reveal the determining factors behind those choices.

Sample: The final sample consists of 107 firms that adopted IAS/IFRS for the first time since the 1st, January 2005, the firms of the SBF 120 index of EURONEXT PARIS.

Model(s): The statistical analysis uses a logistic regression method to attempt to identify systematic differences between firms adopting fair value and others.

Finding: Results suggest that for this French sample of firms, fair value adoption is not linked with size, financial leverage, CEO’s compensation, institutional ownership and cross-listing. Findings show that the majority of French companies maintained historical cost for the valuation of assets, which is the conservative option. French accountants had followed the conservatism principle. So despite introduction of IAS/IFRS standards, which cheer an economic view highlights by the substance over form principle, the traditional conservatism approach stays embedded in French practices.

The Positive Accounting Theory (PAT) is used as an explanatory background. These results raise the question of ability of the PAT for understanding the permanence of historical cost. PAT seems not to explain as we have expected the accounting choice made by French groups during the first adoption of IFRS standards.

We can attribute these results to the particular context of the French transition which can not be inserted in the classical context of the PAT’ research


Objective: In this study they are interested in the degree of uncertainty associated with the settling of a company’s obligations. They identified the degree of uncertainty associated with the settling of a company’s obligations as a proxy for accounting conservatism.

Sample: Their sample consists of 388 business groups from 17 European countries.

Model(s): For these companies they computed the provisions-to-liabilities ratio (PLR) and performed several group tests, according to an original qualitative classification of national accounting cultures.

Finding: They classified the respective countries in three groups, according to how provision recognition is handled by national accounting regulation. Thus, they concluded that there is a certain “domestic accounting culture”, classified as IFRS-compliant, conservative or liberal.

The results indicate that companies incorporated in countries that are classified as ‘conservative’ do attribute a significantly higher degree of uncertainty to their total amount of
liabilities. In addition, it appears that liberal national accounting regulation does not influence companies in departing from the spirit of IFRS. If they take into account that all the companies in their sample prepare their annual accounts in compliance with IFRS, they can conclude that national accounting culture – when classified as prudent – exhibits a significant influence on the IFRS policies that companies apply with regard to the recognition and measurement of provisions. In other words, even if the International Financial Reporting Standards are the common accounting language of listed companies in Europe, the chapter on provisions is still a matter of managerial discretion, being influenced by the traditional accounting practices (conservative).


Objective: This article observes separately and jointly the impact of international financial reporting standards (IFRS) and/or board of directors’ independence, on accounting conservatism in nonfinancial firms between 2002 and 2007.

Sample: They used a sample from the 72 UK nonfinancial firms listed within the FTSE 100 index.


Finding: With regard to the effect of the board of directors’ independence on accounting conservatism, the empirical findings suggest a significantly positive relationship between the percentage of independent directors and accounting conservatism and a significantly negative relationship between the percentages of executive directors and accounting conservatism. Collectively, these findings indicate that a more independent board of directors requires more accounting conservatism. These findings are consistent with the agency theory that posits that accounting conservatism is an important tool in assisting directors to reduce agency and contracting costs.

Moreover, they noted that the constituents of board of directors tend to apply a more conservative accounting, especially after mandatory adoption of IFRS, whereby, in order to achieve higher reporting quality and to reduce agency and contracting conflicts, there was a decline in accounting conservatism caused by IFRS. This result indicates that IFRS and board of directors’ independence have a complementary impact on accounting conservatism and, as a result, corporate governance increases the effectiveness of IFRS adoption concerning accounting conservatism.

Tamer Elshandidy and Ahmed Hassanein found a reduction in conservatism after the mandatory adoption of IFRS, and, also, that board of directors’ independence increased accounting conservatism


Objective: This study investigates the motives of UK listed companies when reporting high and low quality accounting disclosures. It also examines the relation between the quality of published financial statements and earnings management practices, for example, low quality accounting disclosures might be linked to earnings management.

The paper further studies the relation between financial reporting quality and the timely disclosure of losses and difficult-to-verify accounting items, i.e. conservatism. The focus here is on conditional and unconditional conservatism, their association and the variables that influence the asymmetric disclosure of losses.

Sample: The sample consists of 500 UK firms. All sample firms are IFRS users. All sample firms are listed on the London Stock Exchange.

Model(s): The study implements a logit model whereby the explanatory variables are strictly accounting (see Eq. (1)), followed by a logit model, based on Bushee and Miller (2007).

Finding: The findings indicate that firms that display high quality accounting disclosures generally exhibit higher size, profitability and liquidity measures. Firms that experience a change in
management or are audited by a Big-4 auditor also tend to report high quality disclosures. High quality disclosers tend to display higher capital needs and to engage less in earnings management. The study shows that they display greater conditional conservatism and less unconditional conservatism. The findings demonstrate that the conditional form of conservatism is negatively related to unconditional conservatism, as the former tends to enhance contracting efficiency, while the latter might facilitate managerial opportunism. The study provides evidence of asymmetric disclosure of losses for firms with high leverage. The same thing is valid for high quality disclosers that display bad news. In contrast, firms that are in a growth phase are found to provide less conservative and less difficult-to-verify accounting information in order to influence their growth prospects.

11. Charles Piot, Pascal Dumontier, Rémi Janin, (2011), IFRS consequences on accounting conservatism within Europe: The role of Big 4 auditors
   Objective: Charles Piot, Pascal Dumontier, Rémi Janin investigate the effects of IFRS adoption in the EU on accounting conservatism, a feature of earnings quality and contracting efficiency, and the way the large audit firms (Big 4) moderate these effects.
   Sample: They use an extensive database of more than 5,000 IFRS adopters from 22 EU countries, observed over 2001-2008.
   Model(s): They use the Basu (1997) earnings timeliness approach to measure conditional conservatism, and the bias component of the market-to-book ratio to proxy for unconditional conservatism.
   Finding: Their findings run counter to the general expectation that IFRS have contributed to higher accounting quality. The main findings are:
   a) conditional conservatism, as proxied by the asymmetric timeliness of bad vs. good news, has decreased under IFRS for mandatory adopters. Segmented analyses reveal that this effect concerns non-financial industries, timely IFRS adopters – i.e., neither early (voluntary) nor late (mandatory) adopters –, and code-law countries whether they belong to the French, German or Scandinavian legal origin group.
   b) the magnitude of this IFRS effect is positively associated with the distance between IFRS and pre-existing local GAAP;
   c) Big 4 auditors are associated with more aggressive earnings under IFRS, with simultaneous increase (decrease) in good (bad) news timeliness;
   d) unconditional conservatism is higher under IFRS in the presence of a Big 4 auditor; and
   e) mandated IFRS offer a weak contribution to a better comparability of accounting earnings as observed from the timeliness perspective.
   Taken together, these findings suggest that the EU-wide mandatory IFRS adoption has hampered accounting quality.

   Besides this unintended consequence, our findings also suggest that the intended improvements in earnings comparability, put forward by the EC in 2002 at the time of the IAS Regulation, are far from being achieved when looking at the cross-country differences in earnings timeliness. In brief, generalizing the use of IFRS under the one size fits all principle appears to be counterproductive for listed entities, notwithstanding the costs of such an “accounting revolution”.

   Objective: Authors investigated the impact of IFRS adoption on the earnings conservatism as a dimension of reporting quality in Turkey. This study firstly aims to investigate the impact of the change in accounting regime on the earnings conservatism. They provide comparative evidence from (i) historical cost based and (ii) IFRS based reporting samples. Secondly, considering the call to identify the firm specific factors influencing earnings conservatism, they also provide evidence on the impacts of industry (financial and non-financial firms), debt level and firm size.
Sample: The study used data from all firms listed on the Istanbul Stock Exchange (ISE) in the period 1992-2008. The final sample was comprised of 3,789 firm year observations. The study used data from all the firms listed at the Stock Exchange Istanbul (ISE), over period 1992-2008. The final sample comprised 3789 observations firm-years.

Model(s): They use the empirical approach first suggested by Basu (1997).

Finding: The findings of the study lead to the following conclusions:

a) IFRS adoption increased both timeliness and asymmetric timeliness (referring to earnings conservatism) in Turkey.

b) The impact is stronger for financial firms and this might be due to stronger enforcement mechanisms established, after 2001 crises, for financial firms.

c) Firm size and debt level of the firm are negatively related to earnings conservatism, which means larger firms and firms having higher debt levels are less conservative. Additionally, these results are more pronounced under IFRS.

d) Results gathered from panel data analysis are consistent with pooled OLS regression results. However, compared to panel data analysis, pooled OLS regression analysis overestimates the coefficients and sometimes provides even more significant results.

The results of the study show that, IFRS adoption increased both timeliness and earnings conservatism (asymmetric timeliness), the impact is stronger for financial firms, for firms having lower debt levels, and for smaller firms.

4. DISCUSSION AND CONCLUSIONS

The results of the above studies show that as a result of IFRS adoption, conservatism has decreased in general (Paul André, Andrei Filip, 2012; Paul André, Andrei Filip, Luc Paugam, 2013; Cristy Lu, Samir Trabelsi, 2013; Hanna Embring, Johan Wall, 2012; Tamer Elshandidy, Ahmed Hassanein, 2014; Charles Piot, Pascal Dumontier, Rémi Janin, 2011). These findings are consistent with the IASB’s desire that strives to limit conservative accounting practices, considering conservatism as negative bias and threat to neutrality. Thus, conservatism has decreased in countries with strong enforcement / governance, in code law countries; countries of French and German origin law; countries with higher levels of perceived governance, shareholder protection and enforcement; and countries with important debt markets and less developed equity markets. More specifically, the conservatism declined in France, Germany, Greece, Netherlands, Portugal, Spain and Switzerland (Andrew, Philip, 2012).

The decrease in conservatism is most significant in countries which had the greatest difference with the new IFRS standards. Countries for whom IFRS meant the greatest difference in both accounting standards and extra disclosure, experience a reduction in conditional conservatism and countries where tax-book conformity was high, experience, also, a significant reduction in timely loss recognition. The conservatism decline is more significant for firms carrying intangible assets and goodwill in their balance sheets, items for whom the impairment tests rely on fair value estimates. The decrease of accounting conservatism determines the reduction of accounting credibility and implicitly lowers the financial information users’ interest in financial reports prepared under IFRS principles. Therefore, it is better that the accounting conservatism be maintained at a certain level than blindly be lowered (Lu and Trabelsi, 2013). However, although conservatism has decreased, it has not completely disappeared in accounting practices.

In France, despite introduction of IAS/IFRS standards, which cheer an economic view highlighted by the substance over form principle, the traditional conservatism approach stays embedded in French practices (Samira Demaria, Dominique Dufour, 2007). The majority of French companies maintained historical cost for the valuation of assets, which is a conservative option, so French accountants followed the conservatism principle. Other countries with national accounting culture classified as conservative (France, Germany, Switzerland, Netherlands, Finland, Belgium and Austria), has a significant influence on the IFRS policies (Feleagă, Dragomir and Feleagă,
Moreover, that firms that exhibit higher size, profitability and liquidity measures, generally display high quality accounting disclosures. Firms that experience a change in management or are audited by a Big-4 auditor also tend to report high quality disclosures. High quality disclosers tend to display higher capital needs and to engage less in earnings management, they display greater conditional conservatism and less unconditional conservatism (Iatridis, 2011) Do not forget: increasing accounting conservatism is an efficient mechanism to enhance the credibility of information (Cristy Lu, Samir Trabelsi, 2013). Accounting conservatism is preferred because its use helps achieve a more efficient balanced outcome. (Qi Chen, Thomas Hemmer, Yun Zhang, (2007) Furthermore, the conservatism is preferred by debt holders either directly, or if they are price protected, it is preferred by equity holders because they incur the residual agency cost. That conservatism can reduce agency costs and opportunities for earnings management (Gebhardt, Mora and Wagenhofer 2014). Generally, the magnitude of the conservatism reduction is positively associated with the distance between IFRS and pre-existing local GAAP (Charles Piot, Pascal Dumontier, Rémi Janin, 2011). In the countries with weak enforcement /governance there is no change, these countries remain less conditionally conservative than countries with strong enforcement/governance. Cagnur Kaytmaz Balsari, Serdar Ozkan, Mustafa Gurul Durak (2010), show that in Turkey IFRS adoption increased both timeliness and asymmetric timeliness (referring to earnings conservatism). Thus, institutional and legal differences between countries disappear after mandatory adoption of IFRS. The level of conservatism post-IFRS is not significantly different in most EU countries.

We could consider the conservatism decrease determined by the adoption of IFRS as one of the objectives of the IASB, which requires fair value. Therefore, the IASB has achieved one of its objective of smoothing conservatism in all legislations adopting IFRS. Questions arise when it is shown that big companies actually preserved conservative practices (Samira Demaria, Dominique Dufour, 2007). Questions arise when you see the importance of the players involved and the direction in which they move: the states with strong enforcement / governance relinquish the conservative practices (United Kingdom, Norway, Austria, Belgium, Denmark, Finland, France, Germany, Ireland, the Netherlands, Sweden) and countries with weak enforcement / governance bear a slight increase in the level of conservatism (Turkey) or don’t bear any change (Greece, Italy, Portugal, and Spain). We understand, therefore, that accounting practices developed by countries with strong enforcement / governance did not comply with the IASB requirements, which modernized / updated) these accounting practices.

Andre Philip and Paugam (2013) believe that IFRS are conceptually conditional conservative, but it is likely that they were not applied properly, which prevented financial reporting to reach the level of conservatism aimed by IASB. But if all studies lead to the same idea of decreasing conservatism following the adoption of IFRS, it means that the standards developed by the IASB have real limitations regarding conservatism. The IASB argues that the concept of ‘prudence’ has often been misunderstood and that what some people consider prudence is often in fact ‘earnings management’— a deliberate and opportunistic under- or overstatement of earnings—which reduces the quality of the information (Gebhardt, Mora and Wagenhofer 2014).

The decrease of conservatism level following the adoption of IFRS, it may even be agreed upon by the current owner, who can manage thus financial information. Qi Chen, Thomas Hemmer, Yun Zhang, (2007) show that if the accounting information can serves to some dual purposes (i.e., valuation and stewardship purposes), the current owner of a firm has an incentive to engage in earnings management activities in hope of boosting the market price of his firm. But the investors and potential investors, who don’t know the IASB strategy, expect that IFRS implementation would protect them against earnings management.

Although, it seems that in conditions of economic crisis, most companies have increased demand for conservatism, as it happened in 2008 (Lu and Trabelsi, 2013).

Gebhardt, Mora and Wagenhofer 2014 shows that while this is a concern, the IASB could try to re-introduce prudence (perhaps using ‘caution’ instead) for dealing with high uncertainty with a clear definition that separates the concept from opportunistic earnings management. The
Conceptual Framework could be a good way of encouraging or incentivizing the type of conservatism that has been shown to create value for capital providers.

In this paper, we tried to give a literature review on the impact of IFRS adoption on accounting conservatism. We started by presenting definitions of accounting conservatism and clarification of this concept. Then we presented twelve papers studying the impact of IFRS adoption on accounting conservatism as a dimension of the financial reporting quality. In this last part, we presented the evolution of accounting conservatism on different levels that have already been studied by researchers.

We followed to have a picture of the consequences of the IFRS adoption in Europe in order to find which are the demand for conservatism from companies, investors, potential investors and other users of financial information. We found that, following the mandatory adoption of IFRS in Europe, conservatism has generally decreased. However, we found that big companies and investors have a demand to lower accounting conservatism included in the international Financial Reporting Standards. There are proposals for mechanisms of conservatism to be developed within IFRS, under other names than that consecrated, of "prudence". Obviously, these proposals will be the subject of future research.

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SEGMENT DISCLOSURE PRACTICES AND DETERMINANTS: EVIDENCE FROM ROMANIAN LISTED COMPANIES

Ruxandra-Adriana MATEESCU
Ph.D. Student, Bucharest University of Economic Studies
ruxandra.mateescu@yahoo.com

Abstract: This paper aims to be a theoretical but also an empirical study regarding the way listed companies in Romania comply with the requirements of IFRS 8 “Operating Segments”, assessing which is the information companies usually disclose about their operating segments. The second part of the study is dedicated to studying the factors which determine companies to disclose high quality segment information, particular attention is being paid to assessing to what extent does an independently structured board influence the quality of segment reporting or if there are more powerful internal factors that influence the way companies implement this reporting standard.

Keywords: Boards’ independence, institutional investors, Romanian listed companies, Segment reporting

1. INTRODUCTION

The subject of financial and non-financial transparency has gained more and more attention, especially after a series of economic failures, part of them being generated by informational asymmetry problems. That is why worldwide authorities have been making continuous efforts in ameliorating disclosure policies as to permit all stakeholders to build a correct overview.

This study aims, on one hand, to assess the extent to which Romanian listed companies have understood the importance of segment reporting, and how does the implementation of IFRS 8 is being driven in those countries. On the other hand, in an emerging country such as Romania, which is just beginning to implement the International Financial Reporting Standards, it is very important to understand which are the factors that influence companies to comply with the requirements of IFRS 8 and consequently to disclose high-quality segment information.

Particular attention will be paid to the relation between boards’ composition and independence and the segment information disclosure practices. There have been conducted a lot of studies regarding the connection between the boards’ independence and the financial and non-financial disclosure process (Armstrong et al., 2013; Ho and Wong, 2013; Klein, 2002; Patelli and Prencipe, 2007) in many developed countries, but little is known about this very important issue in European emerging countries even though those countries are considered the engine of economic growth, this being the reason why they are nowadays drawing more and more the attention of worldwide researchers. Given the increasing role of the independent board members in ensuring a sound and transparent financial disclosure process, the study will try to determine if the composition of the board does influence the amount and quality of the segment information that companies disclose, or if there are more powerful internal factors, such as company’s size or institutional investors, which drive the implementation of an important disclosure standard, namely IFRS 8 “Operating segments”.

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2. LITERATURE REVIEW

2.1 IFRS 8 “segment reporting” – one step closer to transparency and accountability

Segment reporting has gained important attention in the last years, especially in the context of the increase of the number of worldwide companies and business complexity. In the last years there have been conducted a lot of worldwide studies which have drawn the attention on the increasing importance stakeholders give to receiving high quality business segments information (Nobes and Parker, 2008).

This subject has drawn the attention of the international accounting regulatory bodies. In order to meet the informational needs of the companies’ stakeholders, in 1976, the American regulatory body FASB launched the first set of regulations regarding the segment reporting issues. Five years later, the international homologous body IASC has also launched IAS 14, which required the preparers of the financial statements to use a two-tier approach, requiring disclosure by both line of business and geographic regions (Nichols et al., 2012).

The increase both in business complexity and, consequently, in the financial statements’ users needs has led to a long revision process which had ultimately led to the revision of IAS 14 and to the implementation of IFRS 8 which has replaces this former segment reporting standard. IFRS 8 has taken the managerial approach from SFAS 131, according to which segment reporting is based on those entity components monitored by managers when taking strategic decisions. The specialists’ motivation was that stakeholders should have access to the information the chief operation decision maker (CODM) reviews regularly in allocating resources to segments and when assessing the company’s segments financial results (The KPMG International Standards Group, 2012).

The core principle of IFRS 8 is the disclosure of information that enables users of an entity’s financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environment in which it operates (Ernst & Young, 2009).

IFRS 8 prescribes the way companies should identify their reporting segments and those information which should be disclosed to all the companies’ stakeholders. There are 5 steps which should be followed, namely:

1. Step one: Identification of the Chief Operation Decision Maker (CODM);
2. Step two: Identification of operating segments;
3. Step three: Aggregation of operating segments;
4. Step four: Determination of reportable segments;
5. Step five: Segment disclosure information. (The KPMG International Standards Group, 2012)

Regarding this last step, the most complex of them, IFRS 8 gives detailed information regarding the compulsory information which should be provided for each reporting segment. There are nine types of information which should be disclosed: external revenues, internal revenues (between segments), interest revenue and expense, depreciation and amortisation, other material items of revenue and expense, income tax. Also, entities are required to disclose reconciliation items between the information disclosed in the financial statements and the amounts disclosed for all operating segments, as they are allowed to evaluate the assets, liabilities, revenues and expenses using that basis they use internally, which may be different from the one prescribed by the IAS/IFRS-s.

As previously described, segment reporting is extremely important in helping all stakeholders understand the business as a whole but also analysing all its operating segments in making decisions. There have been conducted many studies especially in developed countries, with great tradition in applying International Financial Reporting Standards, but little is known about the way companies in emerging countries have understood the importance of disclosing high quality segment information.
Given the fact that Romania has recently implemented the International Financial Reporting Standards it is important to discover which is the extent to which listed companies comply with the segment reporting requirements and which is the information companies usually disclose. Moreover, it is also very important to understand what determines Romanian listed companies to disclose more operating segment information, focusing on those internal factors which have a major influence.

2.2 Corporate governance and the importance of transparency

The theme of corporate governance has become of a great concern during the last 40 years, especially after a series of economic failures, which have led to the investors’ loss of confidence in the managers’ ability of best leading the great corporations and public institutions (Cheffins, 2012). There has been an increase in the attention given by worldwide institutions to the improvement of the corporate governance rules and regulations, as to avoid new economic failures and to increase the companies’ accountability towards all their stakeholders.

The Organisation for Economic Cooperation and Development (OECD) has released in 1999 a set of principles, grouped in 6 themes of concern, namely: Ensuring the Basis for an Effective Corporate Governance Framework, The Rights of Shareholders and Key Ownership Functions, The Equitable Treatment of Shareholders, The Role of Stakeholders in Corporate Governance, The Responsibilities of the Board and the last, but not the least, Disclosure and Transparency (OECD Corporate Governance Principles, 2004).

The importance of transparency has been also seized by the European authorities. In 2003, the European Commission has released the Communication 284 (COM-284), which addresses three main issues, one of them regarding the disclosure policies.

Disclosure and transparency issues are also quite important in the emerging countries, which are considered to be the engine of economic growth (Albu et al., 2013). There have been conducted a large number of studies in those countries regarding the importance of the existence of a sound financial and non-financial disclosure system.

One very strong evidence that sustains the importance of a strong disclosure mechanism is a study conducted in Turkey in 2013. Ertuna and Tukel, the authors of this research, have proven the fact that the companies that wish to attract foreign institutional investments usually increase the quality and amount of financial and non-financial information disclosed.

2.3 The connection between the boards’ and independence and the financial and non-financial transparency

As I previously mentioned, nowadays financial and non-financial transparency has gained more and more importance, mostly after a series of long debated financial scandals, many of them generated by the agency problems and by informational asymmetry.

Armstrong et al. (2013) have discovered the fact that even though independent board members have access to internal data and reports provided by companies’ managers, they usually rely more on public disclosed information, given the last years enforcement of the international financial reporting standards. Jesover and Kirkpatrick (2005) also sustain the idea that independent board members have the power and expertise to improve the companies’ disclosure policies, making them more accountable towards all their stakeholders.

Moreover, other studies such as the one conducted by Bianchi et al. in 2011 support the fact that companies where the boards are composed mainly of independent directors tend to be more compliant with rules and regulations, including those regarding disclosure and transparency.

A large number of other studies (Armstrong et al., 2013; Klein, 2002; Patelli and Prencipe, 2007) have shown the fact that the appointment of a larger number of independent
board members is positively related to a decrease in the informational asymmetry materialised in an increase of the quantity and quality of information disclosed by companies.

As an example, a study of Armstrong et al. (2013) concludes the fact that an increase of 18% in the number of independent directors is followed by a 6% decrease in the informational asymmetry existing in the companies. Other studies performed by Klein in 2002, Prencipe and Patelli in 2007 have also shown a positive relation between the board’s independence and the reduction of the asymmetry problems.

Moreover, other studies stand for the importance of an independent audit committee. Ho and Wong (2001) have discovered the fact that companies which appoint an audit committee usually tend to be more transparent. Armstrong et al. (2013) also stand for the fact that when a company increases its number of audit committee independent directors, there is a decrease in the informational asymmetry.

A very important opinion is the one Big4 specialists have regarding the importance the existence and composition of an audit committee has in increasing the quality and amount of information disclosed by companies. Deloitte specialists (2014) support the fact that among the audit committee’s responsibilities, one of the most important is related to review the quality of financial statements and other financial reports, so is expectable to seize a positive relation between the existence and composition of the audit committee and the quality of financial information.

3. RESEARCH METHODOLOGY

3.1 Sample description and data sources

My study aims to discover to what extent companies listed in the first tier of the Bucharest Stock Exchange do comply with the requirements of IFRS 8. Moreover, I will try to seize the factors which influence the segment disclosure reporting practices, paying special attention to assessing the extent to which the board composition influences these practices implemented by the companies in the sample.

The analysed sample is comprised of 15 non-financial companies, listed on the Bucharest Stock Exchange. I chose to eliminate from the analysed sample the banks and other financial institutions (10 companies) in order to maintain the sample’s homogeneity, given that banks and financial institutions have other particular operating segments and consequently other segment reporting practices.

I have taken into account the 2012 annual reports disclosed by the analysed companies, but also other information available on the companies’ websites and on the Bucharest Stock Exchange website.

3.2 Research questions

The first research question will try to find out to what extent Romanian listed companies comply with the disclosure requirements in IFRS 8.

First of all, I will analyse the segment information disclosed by each company, as required by IFRS 8. The compliance has been measured through an index, IFRS8Compliance, inspired by the IFRS 8 requirements and by the Deloitte segment reporting check-list (2007). If a company discloses information regarding one element in the list, the element is “checked” and the index’s value increases by one. In other words, the index is a sum of the “checked” elements presented in the following list, which companies disclose in their annual reports.
- Factors used in determining the operating segments;
- The main products and services which generate revenues for the operating segments;
- Information regarding the main clients;
Revenues obtained from the activities in Romania, respectively in other countries;
- Assets and liabilities related to the activity in Romania, respectively in other countries;
- Each operating segment’s profit or loss;
- Each segment’s assets;
- Each segment’s own liabilities;
- Internal revenues;
- External revenues;;
- Interest revenues;
- Interest expenses;
- Depreciation and impairment expenses;
- Other significant revenues and expenses;
- Operating segments’ revenues valuation basis;
- Operating segments’ assets and liabilities valuation basis;
- Reconciliations between the values disclosed for the segments and those disclosed in the financial segments.

Then, using a four points Likert scale, I will assess the compliance with the IFRS 8 requirements. The way the level of compliance is assessed is described in Fig. 1.

Fig. 1. The IFRS 8 compliance assessment method

Finally, I will try to investigate which are the segment information Romanian listed companies are more willing to disclose.

The second research question intends to discover which are the factors that determine the analysed companies to comply with the requirements of IFRS 8.

Taking into account previous studies (Berglof and Pajuste, 2005; Crawford et al., 2012; Ojo, 2009; Glaum, 2013; Morris et al., 2012; Bonson and Escobar, 2006; Glaum, 2013; Kowalewski et al., 2007; Armstrong et al., 2013; Klein, 2002; Patelli and Prencipe, 2007; Ho and Wong, 2001; Ertuna and Tukel, 2013), I will analyse the influence of 8 internal factors, namely: the companies’ size, profit, percentage of equity held by institutional investors, the type of auditor, the board’s size, the board’s percentage of independent members, the size of the audit committee and the percentage of independent audit committee members.

Based on these previous studies’ results (Berglof and Pajuste, 2005; Crawford et al, 2012; Morris et al., 2012; Bonson and Escobar, 2006; Glaum, 2013; Kowalewski et al., 2007), it is expectable to seize a positive connection between the companies’ size and profitability and the companies transparency, assessed through the IFRS 8 compliance level. According to Morris et al. (2012), more profitable companies tend to disclose more information so that investors can assess better the credibility of their reported earnings and they also tend to increase their voluntary disclosures.

Previous studies (Morris et al., 2012; Bonson and Escobar, 2006; Glaum, 2013) have demonstrated that generally larger audit firms are associated with better financial disclosure, this being the reason why it is expectable to seize a positive relation between the quality of segment reporting and the type of the auditor (Big 4 of not).

It is also expectable to seize a positive connection between a larger presence of institutional investors and the IFRS 8 compliance level, as previous studies (Ertuna and Tukel, 2013) have demonstrated that companies that want to attract more institutional investors usually tend to improve their disclosure practices.
Finally, regarding the size and independence of the board and particularly of the audit committee, it is also expectable to seize a positive connection between these factors and the compliance index, given that previous studies (Armstrong et al., 2013; Klein, 2002; Patelli and Prencipe, 2007; Ho and Wong, 2001) have underlined the connection between the independence and size of the board and audit committee and much more transparent annual reports.

4. RESULTS AND ANALYSIS

Regarding the first research question, out of the 15 companies analysed in the sample, two of them do not mention anything about their operating segments in their annual reports, even though IFRS 8 requires that for all listed companies. Five of the analysed companies have a separate note in their financial statements where they define the concept of operating segment (some of them still disclose the definition in the former segment reporting standard, IAS 14) and state the fact that their activity is unitary, identifying one single operating segment. Only eight companies in the sample (53.33%) sustain the fact that their activity is more diversified, identifying more than one operating segment.

The results of this first research question contradict other European studies. While Nichols et al. (2012) have discovered that 84% of the European listed companies identify operating segments and disclose information regarding their particularities, activity and financial performances, in Romania only 53.33% of the analysed companies are aware of the particularities of their activity and of the existence of more operating segments. One explanation may be the fact that IFRS 8 is being applied only from the beginning of 2009. Another reason may be the fact that Romanian listed companies have a recent history in implementing the International Financial Reporting Standards, given the fact that only since 2012 listed companies must comply with those requirements also in their individual financial statements. Future studies will analyse the coherence between the number of operating segments identified by Romanian listed companies and other information available in their annual reports, websites and other sources.

Fig. 2. The number of operating segments identified by the companies in the sample
Regarding the companies which disclose segment information, they identify in average 2.87 segments, with a maximum of 5 segments. The quite high value of the standard deviation (0.538) shows that there are great disparities between the companies, regarding the number of operating segments. It is possible that some companies are more complex than others, but it may also be possible that companies which identify a few or no operating segments at all do not understand the requirements of IFRS 8, not being able to correctly identify their reporting segments.

<table>
<thead>
<tr>
<th>Number of operating segments (companies which have a separate note regarding the operating segments)</th>
<th>Observations</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Average</th>
<th>Standard deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>13</td>
<td>1</td>
<td>5</td>
<td>2.87</td>
<td>0.538</td>
</tr>
</tbody>
</table>

Fig. 3. Statistical description of the number of operating segments identified by Romanian listed companies

In order to discover which are the types of information companies choose to disclose regarding their operating segments, I will take into account only the 8 companies which have identified more than one operating segment.

Analysing the information companies usually disclose for each reporting segment, as described in Table 4, the results are encouraging. While in Europe 93% of the companies present information regarding the value of each segment’s assets and 71% disclose the segment’s liabilities (Nichols et al., 2012), in Romania, from the 8 companies which have a separate note regarding the operating segments and which identify more than one operating segment, 100% disclose the assets’ value and 87.5% describe each segment’s liabilities.

The least disclosed information are those regarding the interest revenue and expense, given that usually companies treat those elements as a whole, only 50% of the companies which identify more than one operating segments

![Fig. 4. Segment information disclosed by those companies which identify more than one reporting segment](image)

Finally, as I described in the Research Methodology section, I divided the 15 companies in the sample into four categories, taking into account the IFRS8 Compliance index. The results can be found in Figure 5.
These results are also encouraging, especially for a country with little experience in implementing the International Financial Reporting Standards. 40% of the companies in the sample have obtained an over 12 points IFRS8 Compliance score, which means that companies are beginning to understand the importance of high quality segment information. They are being more accountable towards all their stakeholders and this fact equals a signal to the market that they are being more and more transparent and trustworthy.

On the other hand, 33.34% of the companies disclose less than a half of the information IFRS 8 requires, not forgetting about the two companies that disclose absolutely no information regarding their operating segments.

These disparities between Romanian listed companies lead us to the second great research question, regarding the factors which influence companies’ segment reporting practices.

As I previously mentioned, trying to discover the answer to the second research question I will take into account 8 internal factors, as described below.

<table>
<thead>
<tr>
<th>Variables</th>
<th>Measure</th>
<th>Values</th>
</tr>
</thead>
<tbody>
<tr>
<td>Size</td>
<td>Total assets (natural logarithm)</td>
<td>Total values</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Avg 3,595,177 RON</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Min 107,695 RON</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Max 38,144,620 RON</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Natural logarithm</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Avg 13,428 RON</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Min 11,587 RON</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Max 17,457 RON</td>
</tr>
<tr>
<td>Profit</td>
<td>Profit (natural logarithm)</td>
<td>Total values</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Avg 74,866,601 RON</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Max 875,141,108 RON</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Natural logarithm</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Avg 12,008 RON</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Min 0 RON</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Max 20,590 RON</td>
</tr>
<tr>
<td>Institutional</td>
<td>The percentage of equity held by institutional investors</td>
<td>Avg 45,10%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Min 0%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Max 88,42%</td>
</tr>
<tr>
<td>Auditor</td>
<td>Dummy variable, equals 1 if the company is audited by a Big4, 0 otherwise</td>
<td>40% of the analysed companies are audited by a Big4, while 60% are audited by another type of auditor</td>
</tr>
<tr>
<td>BoardDim</td>
<td>The board’s number of members</td>
<td>Avg 6,47</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Min 5</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Max 14</td>
</tr>
<tr>
<td>BoardInd</td>
<td>The percentage of independent board members</td>
<td>Avg 50%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Min 0%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Max 86%</td>
</tr>
<tr>
<td>AuditDim</td>
<td>The audit committee’s number of members</td>
<td>Avg 3</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Min 2</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Max 4</td>
</tr>
<tr>
<td>AuditInd</td>
<td>The percentage of independent audit committee members</td>
<td>Avg 67%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Min 25%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Max 100%</td>
</tr>
</tbody>
</table>

Fig. 6. Variables’ statistical description
The study has also tried to discover a few factors which could influence the segment reporting practices and the amount of information companies are willing to disclose. In order to analyse this fact, I have used a Pearson correlation, whose results are presented below. Out of the 8 internal factors which have been taken into consideration, only three of them are correlated to the IFRS8 Compliance index.

<table>
<thead>
<tr>
<th>Variables</th>
<th>Institutional</th>
<th>Profit</th>
<th>Assets</th>
<th>Auditor</th>
<th>Board Dim</th>
<th>Board Ind</th>
<th>Audit Dim</th>
<th>Audit Ind</th>
<th>IFRS8 Compliance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Institutional</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit</td>
<td>0.462*</td>
<td>1</td>
<td>0.480**</td>
<td>0.371</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assets</td>
<td>0.344</td>
<td>-0.040</td>
<td>0.669***</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Auditor</td>
<td>0.027</td>
<td>0.497**</td>
<td>0.544**</td>
<td>0.199</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board Dim</td>
<td>0.744***</td>
<td>0.272</td>
<td>0.415*</td>
<td>0.275</td>
<td>0.010</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board Ind</td>
<td>-0.222</td>
<td>0.128</td>
<td>0.522**</td>
<td>0.344</td>
<td>0.693***</td>
<td>-0.154</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Audit Dim</td>
<td>0.461*</td>
<td>0.185</td>
<td>0.036</td>
<td>0.118</td>
<td>-0.349</td>
<td>0.222</td>
<td>-0.220</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>IFRS8 Compliance</td>
<td>0.425*</td>
<td>0.047</td>
<td>0.440*</td>
<td>0.569**</td>
<td>0.181</td>
<td>0.074</td>
<td>0.324</td>
<td>-0.024</td>
<td>1</td>
</tr>
</tbody>
</table>

Significant correlation coefficients are indicated in bold. * , **, *** represent p<0.1, p<0.05, p<0.01

Fig. 7. Pearson correlation

As expected, larger companies usually disclose more detailed segment information, sustaining other prior studies (Crawford et al., 2012; Berglof and Pajuste, 2005) which have demonstrated that larger companies are usually much more transparent than other companies. This may be the result of the fact that larger companies tend to attract more investors and help the existing ones in better assessing the company’s financial performance and position.

The positive correlation between the IFRS8 Compliance index and the companies’ size validates the basic assumption of the agency theory.

Secondly, the positive correlation between the IFRS8 Compliance index and Auditor variable validates the results of previous studies (Morris et al., 2012; Bonson and Escobar, 2006; Glaum, 2013; Ojo 2009) which have demonstrated that companies which are audited by larger audit firms are associated with a better disclosure level.

Another important factor which has not been so much studied before is the presence of institutional investors, which resulted to be positively and significantly correlated with the IFRS8 Compliance index. Previous studies (Ertuna and Tukel, 2013) have demonstrated that companies which want to attract institutional investors tend to become more transparent. Moreover, other studies regarding corporate governance issues have also demonstrated that institutional investors have the financial power but also the technical expertise that help companies in implementing better corporate governance mechanisms, including disclosure policies.

Even though there have been conducted a lot of studies (Armstrong et al., 2013; Klein, 2002; Patelli and Prencipe, 2007; Ho and Wong, 2001) which have demonstrated a positive connection between the composition and size of the companies’ boards and especially audit committees, the Pearson correlation presented above shows no significant connection between these corporate governance variables and the IFRS 8 Compliance index. Even though as I previously mentioned a sound corporate governance system influences the companies’ transparency level, it seems that a larger and more independent board does not necessarily imply the disclosure of high quality segment information.
5. CONCLUSIONS

The aim of this study was to assess the extent to which Romanian listed companies have understood the importance of disclosing high quality operating segment information and thereupon the way they have implemented the requirements of IFRS 8.

The results are quite divergent, 33.34% of the studied companies present a low level of IFRS 8 compliance, while 40% of them comply to a high extent with the requirements of IFRS 8.

Regarding the information companies usually disclose regarding their operating segments, the most commonly presented data are those about the segments’ assets, liabilities, external revenues and the segment’s financial result.

Trying to discover the reason why the compliance levels are so different among the companies in the sample, I tested the correlation between the IFRS8 Compliance index and 8 internal variables, namely the assets’ value, the financial result, the type of auditor, the presence of institutional investors, the board’s size, the percentage of independent board members, the audit committee’s size and the percentage of independent audit committee members. The Pearson correlation has proven the fact that only the size, the type of auditor and the percentage of institutional investors have a significant relation with the level of IFRS 8 Compliance.

None of the variables related to the size and composition of the board and the audit committee are correlated with the segment reporting variable, which indicates the fact that probably there are more powerful factors and that maybe, in Romania, managers are the ones in charge with the financial reporting, the board members being implied in other internal activities.

These results lead to a lot of other research questions, the most important, in my opinion, being connected to finding the most appropriate ways of improving Romanian listed companies’ segment disclosure policies.

Concluding the results of this paper, I will cite the opinion of the Deloitte specialists (2014): “The quality of financial and corporate reporting is ultimately determined by the players’ effectiveness in working together as a system. These players, therefore, must consider their own roles and responsibilities and as well as their interaction and working relationships with each other. Such a relationship cannot be forged through simple mechanical or regulated solutions. Instead, the players themselves must develop effective working relationships within their organizations – something that can be done when each player possesses the necessary attributes, expertise and characteristics.”

ACKNOWLEDGEMENT

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CORRUPTION IS PERSONAL –
PROFILING AN ANONYMOUS CRIME

Gabriele MEISSNER
Anglo-American University
gabriele.meissner@aauni.edu

Abstract: We don’t have a good word for the people who choose to engage in corruption, bribery and other corporate frauds like we have for “normal” criminals – i.e. thieves, murderers, and robbers. The description mostly stays somewhat abstract on an organizational level. The ACFE (Association of Certified Fraud Examiners) has published some interesting data on the characteristics of the people who actually commit these crimes. Who are they, what characterizes them, what shapes their decisions? We are looking into the hidden ugly face of corporate and political decision makers in organizations. And it is clear that the available data are only those, which have been made public. This paper will have a closer look at the individuals who choose a path to violate laws, corporate governance, and the economy in general, individuals who refuse to take responsibility for anything else than themselves. It will also have a look at the environment in which corruption in all its many faces thrive. It explores some external influences, which seem to shape individual behavior. In the conclusion some ideas are developed on how to better ensure a valid risk management in organizations, which takes the individual into consideration.

Keywords: corruption, decision makers, crime profile, risk management, organizational culture

1. INTRODUCTION

In 2010 in Germany an elderly care nurse in a home for the elderly was dismissed with immediate effect after 17 years of working there. She ate some food (6 ravioli) which was originally meant for the residents but came back and was about to go to the garbage. Even in the following lawsuit the loss of the job was confirmed; she only had some financial compensation. Eating the food was considered as theft. (ZEIT.de, 2010)

In 2013 the Deutsche Bank dismissed four investment bankers with immediate effect who were involved in the manipulation of the Libor interest rate and thus caused immense damage to the global economy. Also this case went to court, and the Deutsche Bank was forced to re-install the bankers in their former jobs. The court rules the dismissal as “disproportional”. The bankers argued that they didn’t know that they were not allowed to agree on deals with other traders. The Deutsche Bank is still involved in costly international lawsuits. Even though there were not explicit orders concerning the jobs of the bankers, the bank has a code of conduct and corporate governance statements. The bankers also had to get paid the months they were out of job. The lawsuit is ongoing. The judge missed effective control systems in the bank. The Deutsche Bank already had to pay billions of dollars fines. (Süddeutsche.de, 2013)

When we look at these cases we see how easy it is in well paid jobs – management and investment banking for example – to get away even with illegal behavior. Unethical behavior seems to be common ground everywhere meanwhile. The news report almost every day new cases of cartels, corruption or fraud.

2. IMPACT OF FRAUD AND CORRUPTION

The interesting part is not only the fact that fraud in legislation seems to treated differently. Also corruption and fraud in organizations is somehow abstract. The players in this field are mostly
anonymous, and compared to the many cases known on corporate levels comparatively seldom effectively prosecuted on a personal level. The exception seems to be fiscal fraud, but also in these cases the wealthy tend to make deals with the prosecution and walk free. The case of the German football manager Uli Hoeness is an exception, but he reported himself to the tax authorities.

The organizations which are caught in illegal activities pay high fines, and often the individuals who cause the damage walk free or pay some low fines which don’t do much damage. The ex-CEO of the LB Bayern (Landesbank) was just made to 20000 EUR and closing of the proceedings after having caused a damage of 3.7 bn EUR to the bank. His co-executive officers will face similar easy ways out. (Ott, 2014).

It seems the firms willingly pay enormous fines to the EU or US authorities, but in general the actual players are not really affected. So it’s worthwhile to have a look at the individuals who are responsible for these acts of fraud and corruption.

The Association of Certified Fraud Examiners (ACFE) investigated the many faces of fraud and corruption and the players in this field in its 2014 report. It is interesting that we have words for all sorts of crimes – like thief, robber or murderer – but while there are some words for people engaging in fraud (fraudster) there doesn’t seem to be a distinct word for those who are corrupt on the giver and receiver side.

The ACFE could only investigate the cases of known fraud and corruption, the estimated number of unreported cases is much higher. Nevertheless the report gives some clear indicators on the impact of fraud and corruption and the consequences for the individuals involved.

The ACFE Survey participants “estimated that the typical organization loses 5% of revenues each year to fraud. If applied to the 2013 estimated Gross World Product, this translates to a potential projected global fraud loss of nearly $3.7 trillion. The median loss caused by the frauds in the study was $145,000. Additionally, 22% of the cases involved losses of at least $1 million. The median duration – the amount of time from when the fraud commenced until it was detected – for the fraud cases reported to us was 18 months.” (ACFE, 2014)

In general the ACFE lists three different kinds of fraud: corruption, asset misappropriation and financial statement fraud. All of these are often seen as trivial offense, as supposedly nobody is in the end really harmed. It is a bit like insurance fraud in private life – the assumption that we pay insurance rates to get something out of it and the large corporation can afford it anyway. This is a major misconception, as the damage to national economies and also in the end to the organizations in which the fraud happens is huge. The ACFE report states that the most dominant fraud is asset misappropriation, followed by corruption and financial statement fraud. Focusing on Europe, asset misappropriation might have also a cultural background. While Dan Ariely in his book “The honest truth about dishonesty” (2012) reports that cheating tends to be contagious especially in peer groups, some new experiments he conducted in Berlin (Ariely et al., 2014) in cooperation with the Ludwig-Maximilian-University in Munich show that the participants with an East German background seem to be more open to cheating than those from former West Germany which suggests that culture might have a considerable impact. The authors conclude that political and economic regimes might have an even more detrimental impact on human behavior than market decay. Friedbert Hähnel, a former executive manager in one of the East German corporations “Volkseigene Betriebe”, could support this notion. He describes the mentality at the time: as the people own everything, and the employees of the “Kombinat” are part of the people, so they felt entitled to help themselves to the corporate resources. (Hähnel, 2011) As scarcity of consumer goods on all levels was imminent in the political system, we can assume that a similar attitude towards corporate property was also common in other Soviet block countries.

The ACFE analyzed 1483 cases. In about 30% of the cases the fraudsters adopted several overlapping fraud schemes. So corruption and asset misappropriation very often go hand in hand.

It is especially interesting to see how the duration of a fraud scheme affects the damage caused. The longer it lasts, the bigger the damage, the higher the losses.
3. THE ORGANIZATIONS

The next question is how the organizations deal with the attacks. The majority of victim organizations are privately held which lets us assume that SME’s may not have very efficient risk management policies in place. Large corporations follow. While the losses in SMEs are comparatively small (maybe not comparatively to the total volume of business the company does), the large organizations are the real losers here. However instead of introducing a tight risk management and control system most of the organizations wait until they get notified by law enforcement, which maximizes the losses (median loss 1.25 m $ after 30 months of ongoing fraud schemes). (ACFE, 2014)

Banking and Financial Services, closely followed by Government/Public Administration, lead the list of industries of victim organizations.

The most common schemes are also the most risky.

Firms paid huge fines due to the criminal activities of their members. The European Union tries to align its members to fight corruption to enable reliable business standards. Unfortunately, the countries and organizations as well don’t do enough to prevent and detect fraud. Most of them seem to rely on external audits, but at the latest since ENRON everybody knows what the pitfalls are here. Still only few organizations have independent compliance offices to which whistleblowers can report without having to fear negative consequences. The main internal control weaknesses ACFE observed were: lack of internal controls, lack of management review, overriding existing internal controls, poor tone at the top, and lack of competent personnel in oversight roles.
4. THE PERPETRATORS

While the organisations lack efficiency in risk management and as it seems also willingness to proactively address the issue of fraud and related risk, in the end the criminal activity is planned and conducted by individuals. Too often the responsible actors manage to hide behind corporate walls and stay anonymous. So having a look at the personalities who engage in fraud might be worthwhile.

The first question is therefore: who are the people who develop such immense often undetected criminal energy? The ACFE report states that the majority of fraudsters is male with an average age between 30 and 50. This is the preferred age recruiters want for filling management positions. They have at least college degrees, most of them university or postgraduate degrees. They are mostly in senior management positions, and the higher they are the bigger the damage they cause. The perpetrators usually are in the company for at least 1 to 10 years, but the number of cases rises from year 2 on. The list of departments, which are mostly affected by all sorts of fraud schemes, is led by accounting, followed by operations, sales and upper/executive management. The median losses are biggest in Executive/Upper Management, followed by Board of Directors, Finance, Warehouse/Inventory and Purchasing. (ACFE, 2014) The losses increase when more than one perpetrator collaborate. Most of these individuals have no criminal background and have also never been punished or terminated in their jobs.

So what motivates successful people to engage in criminal activities? This is also a question the ACFE report follows up on:
The list seems to be quite obvious, but the question is: Why? Why do people who earn high salaries and bond are in financial difficulties? Why do they think it is necessary to live beyond means? Why misuse close relationships with customers or family to the disadvantage of their employers? So what kind of personalities are we dealing with here?

Gino et al. conducted experiments, which show how contagious environment can be (Gino et al., 2009). The authors conclude that social norms play a major role in determining how people behave. Based on these findings it might be assumed that an organization, which doesn’t bother to implement efficient control systems, is seen by some individuals as an open invitation to help themselves. Cheung at al. analyzed 166 well-known bribery cases and describe, how corruption affects firm value. (Cheung et al., 2012) The authors conclude that the less profitable firms pay the highest bribes without receiving larger benefits. And it seems that the people who are involved in these corruption schemes don’t care if they weaken their employer company considerably, so that in the end it might also mean the end of their employment. It seems that that they feel somehow safe. On the other hand pressure to meet sales and profit forecasts might drive people to desperate actions to overrule dangerous competitors in bids for contracts. In this scenario the shareholder value doesn’t play any role anymore, it is just about winning and of course also cashing in the commission and maybe the promotion for the deal.

When we look at the players in the fraud field we very often find those who are on the “dark side” of personality, which has been explored in a British study with managers. (Furnham et al., 2014) The participants took part in an assessment center. The proposition of the study was that “dark side traits are logically related to vocational values; that is that people with particular dispositions seek out vocational settings that fulfill various drives. What are the “dark sides” of a personality? Mainly an overlapping set of personality traits which D. Paulhus called “The Dark Triad”: Narcissism, Psychopathy and Machiavellianism. “Among the strongest candidates are dis-agreeableness, honesty-humility, lack of empathy (callousness), and interpersonal antagonism.” (Furnham et al., 2013) This implies a fundamental lack of what Daniel Goleman calls social and/or emotional
intelligence. So the lack of empathy in these individuals seems to play a major role. They focus exclusively on themselves, and the issue of “belonging” in a material sense seems to be paramount.

One of the many faces of corruption is rooted in relationships. A recent study reports that “that friendship ties caused directors to be more willing to approve reductions to research and development (R&D) expenses that cause earnings to rise enough to meet the CEO’s minimum bonus target more often than when the directors and CEO were not friends. However, disclosing friendship ties resulted in even greater reductions in R&D expenses and higher CEO bonuses than not disclosing friendship ties. In a second experiment, we find that shareholders were more likely to agree with directors’ decisions to approve cuts to R&D when friendship ties were disclosed.” (Rose et al., 2014) The habit of appointing friends or relatives to corporate positions they are not qualifies for is unfortunately widespread. It seems obvious that people who don’t feel fit for a job try to succeed in any other ways. Financial success, power games - the “dark triad of personality” unfolds here. It is not random that an unwillingness to share duties, irritability, suspiciousness and defensiveness are closely linked to the willingness to engage in fraud. One of the HR related red flags noted by the ACFE report are “Poor Performance Evaluations” and other misconduct. (ACFE, 2014)

Another issue explored by Rose and his co-authors is the impact of stock ownership of directors on firm performance and ethical behavior. The paper states what we have seen in cases like ENRON: “improved performance may not equate with improved governance”. (Rose et al., 2013) The authors conclude: “We conclude that independence requirements resulting from SOX and adopted by the NYSE and NASDAQ focusing on board member affiliation are threatened by directors’ ownership of stock in the companies for which they serve. We suggest that the temptation of stock-owning directors to engage in myopic behavior that could boost the company’s stock price can be mitigated by increasing the transparency of board discussions.” As other studies conclude the welfare of their organizations is not always the driving force of executive managers. We may assume that many people in these positions are also of the “dark side” personality, which includes a high competitive behavior pattern.

Sharma et al. suggest that financial deprivation especially in and after the financial crisis can indeed compromise moral behavior. (Sharma et al., 2014) The experiment conducted by the research team suggests that people who experience financial difficulties don’t change easily their moral beliefs; they tend to apply their moral standards though more flexibly. So some of the issues on the bottom of the list the ACFE report states as reasons for fraud is indeed unexpected financial deprivation.

Many of the “dark traits” are in today’s organizations considered as good personality traits for making a career as managers. Competition, assertiveness, power, charisma – all these traits are often even appreciated by HR managers. There seems to be a lack of awareness about what really makes a good leader on all levels. Thus firms open the doors to potential perpetrators.

5. RISK MANAGEMENT

Rose et al. conducted an experiment to explore “the effects of financial knowledge and dispositional trust on the ability of audit committee members to recognize management attempts to avoid full disclosure to the board and potentially deceive board members.” (Rose et al., 2008) The results match the findings in the ACFE report:

1. the less financial knowledge audit committee members have the more likely are they to accept insufficient information,
2. lack of financial knowledge drives audit committee members to reject sufficient explanation,
3. audit committee members who place high levels of trust in others are more likely to accept insufficient explanations.

If we won’t assume that all auditors who control firms, which somehow “cook the books” are fraudsters themselves, the question remains, which competencies do they really bring to the table. The ENRON case is still well remembered in which the auditing company Arthur Anderson seems to
have just signed the reports. It is still an open political discussion if auditing companies and banks should separate their investment branch from all other banking activities. In general the ACFE report suggests that organizations need to do a lot more to proactively prevent fraud in all its variations. The least they should do are implementing strong and knowledgeable internal control systems, which help them to detect fraud schemes and their actors early.

6. RECRUITMENT AND SELECTION CRITERIA

Coming back to the individuals, risk management starts with selection criteria in the recruitment process. Assessment center offer a wide variety of possibilities to detect the personalities of future employees. The same is true for the existing workforce: before promoting people a development center could give a better understanding of the personality of a candidate than just an interview. It is easy to play a role in an interview, even if it lasts several hours. But keeping the facade up for several days is almost impossible. The “real” personality shows.

I all starts with selection criteria. Paulhus et al. in two recent studies came to the conclusion that “Chronic self-promoters may thrive in job interviews where such behavior is encouraged.” (Paulhus et al., 2013). The magic word here is: encouraged. Many managers, unfortunately also HR managers encourage narcissistic behavior in job interviews. They consider this behavior as engaged and enthusiastic and self-confident. After hiring such a person, there is mostly no further assessment on how the new manager/employee is fitting in. Paulhus and his co-authors suggest that the expertise of interviewers is mission critical for successful interviews. The current practice seems to indicate that either organizations focus on only partly relevant criteria (i.e. young age, low salaries, degrees) or their recruitment process in general is not very structured which is mainly true for SMEs.

7. CONCLUSION

In general it seems that organizations don’t invest much in risk management to detect and avoid fraud. Especially the HR policies don’t seem to take into consideration the possibility that new recruits and managers due to promotion may be “bad apples”. While introducing policies and procedures to make fraud as difficult as possible for these individuals, it seems to be also necessary to have a closer look at the individual in the organization. People who are in positions, which may enable illegal behavior, should be better controlled and also better evaluated beforehand. Assessment resp. development center might be effective. However it all starts with reviewing the selection criteria – for new employees, but also for those who get promoted. Having access to resources might be a powerful temptation for some people.

To protect organizations from their executive managers though shareholders and supervisory boards should put pressure on organizations to install efficient control systems on all levels. Control systems, which cannot easily be overruled. Crime is committed by people, one or more individuals. And maybe it is time to rethink the criteria for good managers and get away from the “dark traits” of personality.

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EMPIRICAL RESEARCH REGARDING RISK AND RISK MANAGEMENT IN ROMANIAN JOURNALS

Elena Mirela NICHITA
Bucharest University of Economic Studies
mirela.nichita@cig.ase.ro

Abstract. The concepts of risk and risk management should be considered an essential part of the leadership team’s decision-making. A lot of studies are dealing with risk and risk management, methods to mitigate risks, avoid risks, classification, and so on. To understand the concept of risk I will take into account the reaction of people to risk as a key factor in assessment of it. In this study I will try to present a history of definition of risk and risk management in accounting, audit, and finance literature. I will prepare my research using social sciences journal indexed as B+ by National Council of Scientific Research (NCSR). The NCSR recognises three categories of journals: A journals (ISI indexed or cited), B+ journals (those indexed in international databases) and B journals (those that meet the score for recognition). Also, I want to identify the roll of accountants, auditors and chief officer in analyzing and reporting risks.

Keywords: accountants, risk, risk management, Romanian Journals

1. INTRODUCTION

In nowadays, both researchers and businessman focus on a new concept Risk Management (RM); all activities are regarded through this new lens. Risk management is more used in insurance and finance fields. Every enterprise has a particular tolerance for risk and strategy for managing it, although few enterprises have a global view of the risks that influence their economic condition. The role of risk architecture is to develop and maintain a framework of the various categories of risk that can affect an enterprise from the perspective of a global economy, national economies, market economies, industry sectors, and individual companies, including creditors, insurers, customers, vendors, and suppliers.

2. HISTORY OF RISK MANAGEMENT

In order to understand the risk management, let’s have a short overview on its etymology:

- Latin: riscum = the challenges faced by sailors on desert (sand storms); (Luhmann, 1993)
- Arabian: risq = everything that God gave you in order to take advantages; (Althaus, 2005)
- Greek: rhiza = (rocky shore) = the full of danger journey of Greek sailors on Mediterranean Sea (van Asselt, 2000)
- Italian: risico (var. rischio) = same, like Latin

As we can see, at the beginning the risk has not only negative components, eventual danger, even the possibility of gain. No matter the origin of term, the risk concept excludes the human responsibility. (Titterton, 2005)

In economic theory, risk refers to situations where the decision maker can assign probabilities to different possible outcomes (Knight, 1921).

Solon, Greek ancient writer wrote the first approach of risk: “There is risk in everything that one does, and no one knows where it will make his landfall when his enterprise is at its beginnings. One man trying to act effectively fails to forecast something and falls into great and grim ruination,
but another man, one who is acting ineffectively a God gives good fortune in everything and escapes from his folly. (Solon, VI century B.C cited by Keown et al., 2005)

Modern era brings new changes upon risk concept: Industrial Revolution, the development of production processes and the statistics (as a new study object) develop the idea that the risk is a consequence of human behavior excluding the faith or luck from risk (Lupton, 1999). So, the risk becomes computable and represent the result of activities develop by people.

Uncertainty – used at the beginnings of modern era – reflects the events that cannot be estimated or events really unknown (Reddy, 1996). The fine line between risk and uncertainty we find it in Keynes writings when discuss about investors behavior in business: the lack of rational thinking is the base of uncertainty, but the risk concept means computation of probability (Reddy, 1996; Tversky & Fox, 1995; Knight, 1921).

The contemporary era excludes positive components of risk, and associates it only with danger, hazard, loss, threats. Lupton & Tulloch (2002) consider that the risk means to live with fear, anxiety, and vulnerability. Risk concept can be assign to any activity with unknown consequences. The findings of Blaxter (1999) show how and in which filed the researchers use risk concept:

- Individual Health = 41 %
- Social welfare = 16%
- Organizations management = 10%
- Public services = 10%
- Financial = 8%
- Personal options (as individual) = 4%
- Abstract (theory) = 11%.

Althaus (2005) considers risk as part of any science/domain, as follows:

<table>
<thead>
<tr>
<th>Domain</th>
<th>Perspectives on Risk</th>
<th>Solution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Engineering science, mathematics</td>
<td>Computable item</td>
<td>Computations</td>
</tr>
<tr>
<td>Physique, biology, medicine</td>
<td>Objective reality</td>
<td>Principles, computations</td>
</tr>
<tr>
<td>Law</td>
<td>Mistake</td>
<td>Rules, norms</td>
</tr>
<tr>
<td>Linguistic</td>
<td>Concept</td>
<td>Terminology, meanings</td>
</tr>
<tr>
<td>History, human sciences</td>
<td>Novels, stories</td>
<td>Narratives</td>
</tr>
<tr>
<td>Art (literature, music, poetry, theatre)</td>
<td>Emotion, feelings</td>
<td>Emotion</td>
</tr>
<tr>
<td>Religion</td>
<td>Faith</td>
<td>Revelation</td>
</tr>
<tr>
<td>Philosophy</td>
<td>Debatable phenomena</td>
<td>Wise</td>
</tr>
<tr>
<td>Audit</td>
<td>Computable item</td>
<td>Computations</td>
</tr>
<tr>
<td>Accounting</td>
<td>N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

Source: Althaus (2005), A Disciplinary Perspective on the Epistemological Status of Risk

3. RISK MANAGEMENT IN BUSINESS FIELD

Business risk management, taking a variety of forms, has been a growth point in corporate management in recent years. That change in emphasis is said to stem from responses to high-profile disasters.

Within companies we discover the link between goals, risk analysis and continuity of activities. For more comprehensive understanding, the figure is suggestive.
Fig. 1. Inclusion of risk in business

In order to improve public services, the National Audit Office from London realized a survey in 2000 to identify the barriers and incentives that businesses apply in their activities and public institutions should pay attention:

<table>
<thead>
<tr>
<th>Barriers to effective management of risks</th>
<th>Incentives to encourage risk taking</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ Risk averse culture</td>
<td>✓ Better recognition and reward schemes for</td>
</tr>
<tr>
<td>✓ Lack of a culture which appreciates risk and</td>
<td>✓ Initiative, innovation and well managed risk</td>
</tr>
<tr>
<td>✓ risk management</td>
<td>✓ taking</td>
</tr>
<tr>
<td>✓ There is a blame culture within the</td>
<td>✓ Top management remove the blame culture</td>
</tr>
<tr>
<td>✓ department</td>
<td>✓ And fear of failure</td>
</tr>
<tr>
<td>✓ Risk taking is difficult in the public sector</td>
<td>✓ Clear leadership by example</td>
</tr>
<tr>
<td>✓ Lack of awareness about risk management</td>
<td>✓ Encouragement from the board/senior</td>
</tr>
<tr>
<td>✓ Lack of time and resources</td>
<td>✓ management</td>
</tr>
<tr>
<td>✓ Lack of training, knowledge and formal risk</td>
<td>✓ Better training, involvement and education in</td>
</tr>
<tr>
<td>✓ management tools</td>
<td>✓ risk management</td>
</tr>
<tr>
<td>✓ Lack of clear guidelines for staff</td>
<td>✓ Innovation award schemes</td>
</tr>
<tr>
<td>✓ Uncertainty over funding</td>
<td>✓ Individual accountability for results and</td>
</tr>
<tr>
<td>✓ Absence of a risk management strategy or policy</td>
<td>✓ achievements</td>
</tr>
</tbody>
</table>


Recent decades have witnessed a massive growth in academic studies of risk and the rapid development of a risk industry (Gabe, 2013). The elements of risk-based approaches are various. At a minimum they entail the use of technical risk-based tools, emerging out of economics (cost-benefit approaches), and science (risk assessment techniques). Hood et al (2001) refer to this as a move to a “cost benefit analysis culture” that is a move away from informal qualitatively based standard setting towards a more calculative and formalized approach. Integrated and more holistic approaches to regulating risks may be involved; this involves co-ordinate approaches to risk management which conceptualize risks as interrelated to each other and as having potential consequences for broader economic, natural, social and political environments.

4. MILESTONES IN RISK MANAGEMENT PUBLICATIONS

The first academic books about risk management were published by Mehr and Hedges in 1963 and Williams and Hems in 1964 (Dionne, 2013). Their content covered pure risk management, which excluded corporate financial risk. Initially, risk management was applied in insurance area, but the evolution of society imposes to use it in many other domains. The first use of Brownian motion in financial area by Bachelier in1900 is considered the birth of modern financial theory. The American Finance Association met in 1932 published in 1942 its first journal American Finance, that will
became in 1946 the known *The Journal of Finance*. American Risk and Insurance Association set up in 1932 and published, starting 1964 *Journal of Risk and Insurance*. Other important journals are *Risk Management* under Risk and Insurance Management Society association and *The Geneva Paper or Risk and Insurance* by Geneva Association. After World War II, large companies with diversified portfolios of physical assets began to develop self-insurance against risks, which they covered as effectively as insurers for many small risks. Self-insurance covers the financial consequences of an adverse event or losses from an accident (Erlich and Becker, 1972; Dionne and Eeckhoudt, 1985). The increase of financial instruments (derivatives) more after 1970 is another reason of evolution of risk. The investors tried to minimize their loss by creating mixed portfolios. The most important studies about risk on financial markets were published in *Journal of Finance*; the researchers Markowitz, Lintner, Treynor, Sharpe, and Mossin developed Capital Asset Price Model (CAPM) and were rewarded with Nobel Prize. Black and Scholes’s model is undoubtedly the most popular of these early models. These authors were the first to propose an explicit formula for the pricing of a derivative, namely an option. The bank JP Morgan developed the Risk Metrics and Credit Metrics, highlighted the idea of measuring risks in portfolio form by considering their dependencies and using value at risk quantifying aggregate portfolio risk. These models contribute to create another concept *Value at Risk* (VaR) defined as maximum value that a portfolio or company can lose during a given period of time, at a specified level of confidence.

The financial crisis and big losses from derivatives determined the regulatory bodies to issue rules for risk management in banks under the name Basel I (1988), Basel II (2004), Basel III (2010) and Solvency I and Solvency II (2009) for insurance companies.

The important moments of risk and risk management are presented below:

<table>
<thead>
<tr>
<th>Year</th>
<th>Event</th>
</tr>
</thead>
<tbody>
<tr>
<td>1730</td>
<td>First futures contracts on the price of rice in Japan</td>
</tr>
<tr>
<td>1864</td>
<td>First futures contracts on agricultural products at the Chicago Board of Trade</td>
</tr>
<tr>
<td>1900</td>
<td>Louis Bachelier’s thesis “Théorie de la Spéculation”; Brownian motion</td>
</tr>
<tr>
<td>1932</td>
<td>First issue of the <em>Journal of Risk and Insurance</em></td>
</tr>
<tr>
<td>1946</td>
<td>First issue of the <em>Journal of Finance</em></td>
</tr>
<tr>
<td>1952</td>
<td>Publication of Markowitz’s article “Portfolio Selection”</td>
</tr>
<tr>
<td>1961–1966</td>
<td>Treynor, Sharpe, Lintner and Mossin develop the CAPM</td>
</tr>
<tr>
<td>1963</td>
<td>Arrow introduces optimal insurance, moral hazard, and adverse selection</td>
</tr>
<tr>
<td>1972</td>
<td>Futures contracts on currencies at the Chicago Mercantile Exchange</td>
</tr>
<tr>
<td>1973</td>
<td>Option valuation formulas by Black and Scholes and Merton</td>
</tr>
<tr>
<td>1974</td>
<td>Merton’s default risk model</td>
</tr>
<tr>
<td>1977</td>
<td>Interest rate models by Vasicek and Cox, Ingersoll and Ross (1985)</td>
</tr>
<tr>
<td>1980–1990</td>
<td>Exotic options, swaps and stock derivatives</td>
</tr>
<tr>
<td>1979–1982</td>
<td>First OTC contracts in the form of swaps: currency and interest rate swaps.</td>
</tr>
<tr>
<td>1985</td>
<td>Creation of the Swap Dealers Association, which established the OTC exchange standards</td>
</tr>
<tr>
<td>1987</td>
<td>First risk management department in a bank (Merrill Lynch)</td>
</tr>
<tr>
<td>1988</td>
<td>Basel I</td>
</tr>
<tr>
<td>Late 1980s</td>
<td>Value at risk (VaR) and calculation of optimal capital</td>
</tr>
<tr>
<td>1992</td>
<td>Article by Heath, Jarrow and Morton on the forward rate curve</td>
</tr>
<tr>
<td>1992</td>
<td>Integrated Risk Management</td>
</tr>
<tr>
<td>1992</td>
<td>RiskMetrics</td>
</tr>
<tr>
<td>1994–1995</td>
<td>First bankruptcies associated with misuse (or speculation) of derivatives: Procter and Gamble (manufacturer, rates derivatives, 1994), Orange County (management funds, derivatives on financial securities, 1994) and Barings (futures, 1995)</td>
</tr>
<tr>
<td>Year</td>
<td>Event</td>
</tr>
<tr>
<td>--------</td>
<td>----------------------------------------------------------------------</td>
</tr>
<tr>
<td>1997</td>
<td>CreditMetrics</td>
</tr>
<tr>
<td>1997–1998</td>
<td>Asian and Russian crisis and LTCM collapse</td>
</tr>
<tr>
<td>2001</td>
<td>Enron bankruptcy</td>
</tr>
<tr>
<td>2002</td>
<td>New governance rules by Sarbanes-Oxley and NYSE</td>
</tr>
<tr>
<td>2004</td>
<td>Basel II</td>
</tr>
<tr>
<td>2007</td>
<td>Beginning of the financial crisis</td>
</tr>
<tr>
<td>2009</td>
<td>Solvency II (not yet implemented in April 2013)</td>
</tr>
<tr>
<td>2010</td>
<td>Basel III</td>
</tr>
</tbody>
</table>


5. RESEARCH METHODOLOGY AND SAMPLES

My study proposes to prepare an analysis of journals and papers related to risk and risk management in Romanian Journal. In order to achieve this goal I started with a short analysis of international journals related to risk and risk management, using SRJ journals data base. The flow to select journals start with:

1. Journals that have in their name the noun risk;
2. Eliminate journals with words compound the noun risk (depending the language);
3. Eliminate the proceedings and conferences volumes.

Applying these rules I obtain 41 journals, shown in Annex 1. The structure by country reveals that UK is the leader in risk journal publishing followed by USA and New Zealand. All these countries (Anglo-Saxon type) cover 75% of journals.

<table>
<thead>
<tr>
<th>Country</th>
<th>No of journals</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK</td>
<td>21</td>
<td>51.22%</td>
</tr>
<tr>
<td>USA</td>
<td>6</td>
<td>14.63%</td>
</tr>
<tr>
<td>New Zealand</td>
<td>4</td>
<td>9.76%</td>
</tr>
<tr>
<td>Sweden</td>
<td>3</td>
<td>7.32%</td>
</tr>
<tr>
<td>Nederland</td>
<td>3</td>
<td>7.32%</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>1</td>
<td>2.44%</td>
</tr>
<tr>
<td>Denmark</td>
<td>1</td>
<td>2.44%</td>
</tr>
<tr>
<td>Spain</td>
<td>1</td>
<td>2.44%</td>
</tr>
<tr>
<td>Germany</td>
<td>1</td>
<td>2.44%</td>
</tr>
<tr>
<td>TOTAL</td>
<td>41</td>
<td>100%</td>
</tr>
</tbody>
</table>

Source: Author Analysis
Taking into account the field of journal, the distribution is shown in the below:

<table>
<thead>
<tr>
<th>Domain</th>
<th>No of journals</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medicine</td>
<td>17</td>
<td>41.46%</td>
</tr>
<tr>
<td>Business, Management and Accounting / Economics, Econometrics and Finance</td>
<td>7</td>
<td>17.07%</td>
</tr>
<tr>
<td>Environmental Science</td>
<td>7</td>
<td>17.07%</td>
</tr>
<tr>
<td>Engineering / Environmental Science</td>
<td>3</td>
<td>7.32%</td>
</tr>
<tr>
<td>Decision Sciences / Arts and Humanities / Social Sciences</td>
<td>2</td>
<td>4.88%</td>
</tr>
<tr>
<td>Earth and Planetary Sciences / Engineering</td>
<td>2</td>
<td>4.88%</td>
</tr>
<tr>
<td>Agricultural and Biological Sciences / Pharmacology, Toxicology and Pharmaceuticals / Medicine / Chemistry / Environmental Science</td>
<td>1</td>
<td>2.44%</td>
</tr>
<tr>
<td>Education</td>
<td>1</td>
<td>2.44%</td>
</tr>
<tr>
<td>Social science</td>
<td>1</td>
<td>2.44%</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>41</strong></td>
<td><strong>100.00%</strong></td>
</tr>
</tbody>
</table>

Source: Author Analysis

For Romania, the research is based on social sciences journals indexed as A and B+ by the National Council of Scientific Research (NCSR). The NCSR recognises three categories of journals:
- A journals (ISI indexed or cited);
- B+ journals (those indexed in international databases);
- B journals (those that meet the score for recognition).

Because my interest is in accounting area, the selected journals are in economic field. For this research I chose the journals published by the most important universities from Romania, with headquarter in Bucharest, Cluj Napoca, Iași, Sibiu and Timișoara.

Applying the mentioned criteria, I obtained a sample of 10 journals:
- 1 A journal (ISI indexed);
- 9 B+ journals.

The total number of articles/papers is:

<table>
<thead>
<tr>
<th>Journal</th>
<th>No of papers</th>
</tr>
</thead>
<tbody>
<tr>
<td>A journal</td>
<td>14</td>
</tr>
<tr>
<td>B+ journals</td>
<td>61</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>75</strong></td>
</tr>
</tbody>
</table>

Source: Author Analysis

For a qualitative analysis I grouped the selected paper in 8 categories, as follows:
- Risk in management;
- Risk in IT area;
- Risk associate with financial market and financial instruments;
- Risk in bank and insurance sector, included banking audit;
- Risk in financial and internal audit;
- Risk in agriculture and environmental area;
- Risk as an abstract item (theory).
- Other subjects.
The structure is presented below:

<table>
<thead>
<tr>
<th>Journal</th>
<th>Management</th>
<th>IT</th>
<th>Financial market &amp; instruments</th>
<th>Bank &amp; insurance</th>
<th>Financial and internal audit</th>
<th>Environmental area</th>
<th>Theory</th>
<th>Other</th>
</tr>
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Source: Author Analysis

I have to mention that is possible like one paper to be suitable to another category; when I established the classification for each one I took into account the main content of it; it is difficult to distinguish between IT and bank, when a paper discuss the relevance of IT for bank system. The paper is a qualitative research and there is a subjective influence.

a. Risk in management area

In their paper, Ganea & Ioţa (2014) debate the credit period for receivables and payables and the solutions to improve the operational activity. To compute the commercial risk, they propose a score function to compute the optimal period for sales on credit and purchases on credit. Price Water House Coopers (2014) conducted a survey to identify the opportunities for new strategies: talent management and the organizational structure will be the target. The Romanian CEOs are more confident than European, but their concerns refer to unsecure economic growth, exchange rate volatility, Government policies regarding the taxations. The study revealed the intention of CEOs to improve the relationships with customers, stakeholders and local communities. Based on a sample of 36 companies and a period between 2002 and 2009, Karaka and Savsar (2012) analyzed the food,
drink, tobacco, and basic metal industries and concluded that financial ratios affect the value of firm being a significant and negative relation between inventory turnover and return on equity. The paper of Minárová (2012) provides detailed explanation of the procedure used to calculate the Somers' d coefficient (calculated using partial calculations of the number of concordant and discordant pairs). The author tries to identify the options for obtaining incentives for risk management in logistics; the survey was conducted in Czech Republic and Slovakia in 2010. In order to obtain financing, the companies have to make correct decisions (Ilie, 2011). The appropriate scenarios for companies facing the uncertainty and market risk are based on forecasting (Doval, 2010). The chance of winning or risk of losing the essence of business is because the success in business is dependent not only on quality management but also the evolution on market conduct and business partners (Bogdan, 2009). Bogdănoiu (2008) recommends a high level of prudence in any type of business because the insufficient knowledge of risk, it wrong evaluation, the missing of an appropriate protection against it, will affect directly the final result of carry on activity.

b. Risk in IT area

Models for prediction of bankruptcy proposed by Păvăloaia (2013) are based on combination of three items: web, excel sheets and expert systems and he intent to offer free access to models. He applied the model for small and medium entities. Bonson (2008) analyze the way in which the insurance industry is confronting the renewal of its regulatory framework with respect to the levels of solvency that insurance entities should maintain, and how technological initiatives in general, and the implementation of the eXtensible Business Reporting Language (XBRL) mark-up language in particular, are making a key contribution to the process of adaptation to the new regulation. He concludes that the XBRL will improve the reporting in insurance companies and a better risk assessment and he encourages the utilization of XBRL language. Another paper about advantages of XBRL in audit was published by Eni & Năstase (2013); they mention the possibilities offered by XBRL to extract useful information for auditors from financial statements and help them in their procedures, especially related to risk.

c. Risk on financial market

A lot of writers are interested by financial markets and they conducted papers will very high level of quality. Horobeţ (2010) considers that the underestimation of risk comes largely as a result of two realities: first, risk magnitude was not entirely known by market participants, due to an interlinking of securities, structures, and derivatives built around the subprime mortgages; second, market participants ignored these risks to a large extent, in a world were access to financial markets was as easy as never before. Horobeţ & Ilie (2009) analysed the contribution of exchange rate risk to the risk of an international investor diversified in his home market and the Romanian market and observed that the risk is small, even negative, with no significant differences turbulent versus normal times. Another paper published by Horobeţ & Dumitrescu (2008) related to the exchange rate and the exposure to changes in the nominal and real exchanges rates of the local currencies that companies from a number of four Central and Eastern European countries (Romania, Hungary, Czech Republic and Poland) find limited evidence for contemporaneous and asymmetric exposure to nominal and real exchange rate risk in all four countries, but consistent evidence for three to four months lagged exposure. Horobeţ & Belascu (2012) use a sample of companies listed on first and seconds tier on Bucharest Stock Exchange for 8 years between 2002 and 2009 and applying DuPont system they concluded that the Romanian companies are not able to offer investors constantly good risk-adjusted returns. A comparative study on emerging markets (from EU or outside EU) conducted by Păun et al. (2008) is based on positive relationship between risk and return. The risk mitigation using derivatives is analysed by Şontea & Stancu (2011), Mionel & Moraru (2013), Chirilă & Chirilă (2014), Huian (2014), Şerban, Ştefânescu & Ferrara (2013). All the papers create
meta-models for portfolios based on Markowitz, Scholes models applied on companies traded on Bucharest Stock Exchange. The most common financial instruments on Romanian market are swap contract on interest rate and exchange rate. To answer to the question “The risk-return trade-off in Europe is there a pro-cyclical risk aversion?” Arago & Salvador (2012) conducted their paper based on 15 industries (automobiles, banks, basic resources, chemicals, construction, energy, financial services, food & beverage, health & care, industrial, insurance, media, technology telecommunications, utilities) and 1130 weekly observations. The results revealed a positive and significant relationship between return and risk using multivariate GARCH, cross-sectional analysis, and ICAPM methodology, in the same time they discover no favorable evidence when we use a single portfolio; so, this methodology let them overcome the disappointing results when we focus narrowly in a single portfolio.

d. Risk in banks and insurance area

Related to these sectors, the authors focused on Basel accord and/or Solvency accord (Butaci, 2010; Barreira, Pryer & Tang, 2009; Naghi, 2013; Dardac & Grigore, 2011). Banks may use internal models to determine minimum capital requirements imposed by new regulations to be adopted gradually in the period 2013-2019. In this context, the implementation of internal models by banks, applying VaR or ES risk measures, is a challenge both in terms of continued growth in the number of methods used and the complexity of practical approaches. Dardac & Grigore (2011) propose to estimate the market risk by VaR and ES risk measures using parametric methods, nonparametric and Monte Carlo simulations and implementation of stress tests to assess the capital adequacy under stressed macroeconomic environment. Butaci (2011) considers that regulation of financial services should be reviewed to be modernized and more harmonized. Ilie (2011) developed a new approach for credit risk analysis because superficiality and incompetence demonstrated by the banking system in credit risk analysis has seen the highest peaks. Mierzejewski (2008) demonstrated in his paper that then an optimal level of capital exists, which is characterized in terms of the actuarial prices of the involved agreements, the capital structure of firms that cannot hedge continuously being affected by the agency costs and the moral-hazard implicit in the contracts they establish with stockholders and customers. A critical analysis of credit risk is prepared by Vasilescu, Sitnikov & Fota (2006) and highlight that the credit risk’s potential was over dimensioned by the various evolutions of the companies and their debt level. Voinea & Anton (2009) consider that financial risk management has gained an important role for the companies and financial institutions, due to the fact that financial innovations have improved the efficiency of risk management process, but at the same time, they have imposed new challenges for market participants and their supervisors in the areas of systemic risk. The concept of “shadow banking system” (defined by Paul McCulley as financial intermediaries with a high financial leverage, whose liabilities are perceived, generally, as similar with good money, with a liquidity similar to the conventional deposits) is the core of Petria paper (2012); the solutions to prevent the negative effects of the action of shadow banking system are revealed: need of collaboration and coordination at global level for these measures to be effective, and a need of political determination and will to be put into practice. The new discovers in many areas and the request of entities to finance the research and develop costs create for bank new challenges in order to control and measure risk in these kind of projects (Morariu & Petroianu, 2013).

e. Risk in financial and internal audit

Risk in audit is very important; IFAC developed an international standard about risk ISA 315 (Revised) Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment.

Fraud risk is analysed by Coracioni (2013) using Benford model. Robu & Robu (2013) aim to evaluate fraud risks conditioned by accounting window dressing techniques, using Beneish...
indexes; the paper has a sample of 64 listed companies on Romanian market during 2010-2012. The changes in Financial Reporting proposed by International Accounting Standard Board rose a question for Hudgson & Nechita (2013) who try to explain the auditors the comprehensive income and to highlight the vulnerable risk zone of it. Return rates applied by Jaba et al (2013) on a survey of 50 listed companies on Bucharest Stock Exchange and New York Stock Exchange reveals high differences between companies with greater leverage and small leverage. Leverage is considered a stressful factor for many companies.

The goal of internal audit is to mitigate the risk and improve the processes. Every company aims at implementing the three desiderata, namely corporate governance, risk management and internal control system, thus the internal audit is the key component of this corporate ideals surveillance but it also has an important role in management education, in finding efficient solutions (Onica, 2013). The risk management techniques represent the support needed for the maximization of the company values, also providing help to the objectives of corporate governance. The financial control of the managers’ activity represents an important part of a corporate governance code and it consists of minimal requirements for the managers and executive officers (risk exposure, performance indexes, etc.), for censors and auditors (employment, payment etc). The need to improve techniques for risk in audit is request by Popa et al. (2013) in their paper. Risk assessment of internal control is an assurance that changes will be made safe, that that will be monitored. Changes have a greater impact on internal auditors and managers that show greater sensitivity to risk (Ghiță, 2009).

f. Risk in agriculture and environmental area

In my sample I have two papers included in category Risk in agriculture and environmental area. The authors try to quantify the polluting phenomena in the air and various measures of risk to quantify it for 4 companies from automobile, steel, chemical and cement industry (Galupa, Albu, Hartulari, 2011). To measure the degree of risk of environmental pollution, they suggest a multidimensional model, with 4 parameters:
- T time, with its members: year, season, month, day;
- L location, with its members: developments regions, administrative regions, economic units;
- P polluting factors, with its members: type (air, water earth), code name, unit measure, alarm threshold, alert threshold;
- E the experimental data gathered, with its members: type of test, category of polluting factor, location, time and frequency.

Di Gisi (2010) debates the risk of accidents and technical failures on major gas import pipelines.

g. Developments of risk in theory

An original model for risk estimation and optimization which has the advantage of being easy to be implemented and to be solved is developed by Dedu & Fulga (2011); their model was tested for a set of companies listed on Bucharest Stock Exchange. They consider that finding relies in the fact with minimization problem that can be solved using linear programming techniques. Even though it provides a sub-optimal portfolio, it proves good results in practice. The three methods by which VaR can be calculated: the historical simulation, the variance-covariance method and the Monte Carlo simulation are analysed by Stancu & Balu, describing the advantages and disadvantages, facilitating the understanding of concept. They conclude that on Romanian market only the banks and large companies use it.

h. Risk in other domain

Other papers not included in none of the above area are dealing with risk in fiscal policies in Kosovo (Kida, 2013) or mutual funds performance (Tanja & Uros, 2013).
6. CONCLUSIONS AND FINAL REMARKS

The aim of this research is to examine the Romanian literature regarding the risk management. The paper is based on a small number of papers, because this concept is not very used by companies in our country. Most of the papers present the empirical cases using the listed companies on financial market; other important category is related to audit because the risk has an international standard. In accounting, the risk concept is connected to provision, and the International Accounting Standards Boards in its Glossary defines risk using tautology approach. The regulations of risk are addressed to bank and insurance companies. There is a strong relationship between risk and subjectivity: the people construct risk knowledge in context of their day – by – day events. Risk management should increase the value of a company and to become a part of company governance. This research is the start of the innovative idea to bring risk in accounting and to develop a model for risk assessment for an accounting services entity; this will be a great challenge and an opportunity for future.

ACKNOWLEDGEMENT
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ON FINANCIAL MARKETS INFRASTRUCTURES REGULATED DEVELOPMENT

Vladislav PAVLAT
University of Finance and Administration, Prague, Czech Republic
vladislav.pavlat@vsfs.cz; v.pavlat@volny.cz

Abstract: The aim of the paper is to describe and analyse the present state of international efforts to increase the efficiency of financial markets infrastructures (FMIs). The experience of the last financial crisis, its negative impact on financial markets (FM) and FMIs has been a strong motive for an upgrade FM and FMIs regulation and supervision. In part I. of the paper FMIs and their role is defined. Part II gives a brief characteristics of international organizations supporting the internationally co-ordinated development of FMIs and theirs regulation. The analysis shows that the level of international co-operation, co-ordination and harmonisation achieved in the area of different FMIs differs. In Part III., IOSCO activities on the field of specific FMIs which are crucial for further FM development are analysed. Present results of IOSCO co-operation with other international organisations are discussed.

Keywords: financial markets infrastructures (FMIs), FMIs regulation, international organizations’ co-operation

JEL Codes: G 17; E 44.

INTRODUCTION

The objective of this paper is to characterize the FMIs, the relationships between financial markets and financial market infrastructures, and the need of FMIs regulated development, both at the national and the international level.

Since the burst out of the world financial and economic crisis, a new approach to the financial market infrastructure has been adopted and new principles for these infrastructures and their regulation applied.

In the process of the international FMIs regulation many international organizations are involved. In this paper the historical development of the international co-operation on the field of FM and FMIs is highlighted. The IOSCO and its important role during the world financial and economic crisis are analysed.

1. FINANCIAL MARKETS AND FINANCIAL MARKETS INFRASTRUCTURES

Financial market infrastructures definitions used to characterize the vast “world” of products, services, institutions and organizations the existence of which is absolutely indispensable for financial markets widely differ.

1.1 Definitions of FMIs

Financial markets do not function in a vacuum – they operate within a specific time and place. Therefore, they require certain conditions to operate, referred to as the “financial market infrastructures”. In this regard, the financial market infrastructures can be defined as follows: 1) As a set of material-technical conditions, required for the functioning of financial markets; 2) As a set of activities, which must be performed to allow trading of financial assets on the financial markets;
and 3) As a group of institutions and organizations necessary for smooth operation of financial markets (Pavlát, 2013).

Generally speaking, the financial market infrastructures may be considered as a “superstructure” of the financial markets with their direct participants, whereas such superstructure should facilitate the financial market functioning – both directly and indirectly.

In literature, many different general definitions of the world “infrastructure” can be found. Our above definition represents an application of FM theory and belongs to the “academic” definitions which frequently are criticized by practitioners, because it is not always possible to use such definitions in practice. This is the reason why the IOSCO empirical definition is used in this paper.

1.2 Basic types of FIMs according to the IOSCO definition

The IOSCO Technical Committee defines the financial markets infrastructures as “a multilateral system among participating financial institutions, including the operator of the system, used for the purposes of recording, clearing, or settling payments, securities, derivatives, or other financial transactions.” (CPSS – IOSCO, 2011a)

According to the IOSCO (“narrow”) definition, 5 basic types of the financial market infrastructures are distinguished: 1) Payment systems (PS); 2) Central securities depositories (CSD); 3) Securities settlement systems (SSS); 4) Central counterparties (CCP); 5) Central electronic databases of electronic transactions (Trade Repositories – TR). (CPSS – IOSCO, 2012a)

Since the above mentioned classification is relatively new, let us specify brief characteristics of individual components of the financial market infrastructure system (CPSS – IOSCO, 2012b).

Payment systems are the first component in the classification of the financial market infrastructures. A payment system may be viewed as a network of relationship between/among institutions, instruments, rules, work procedures, standards, and technical measures that allows financial payments in economy. Parties to transactions may settle their mutual payment obligation via a payment system. However, a payment system may only work, if the relevant legal regulations and technical standards are followed. Under the historical development of payment systems, a maze of heterogeneous methods of payment execution has emerged, the organization of which underwent the process of creating internationally applicable payment execution method in the past century, supported by the process of harmonization of legal regulations as well as the process of procedural and technical standardization. The recent global financial crisis has made new, more effective approaches to the regulation of payment systems necessary, both on the national payment system level and the international payment system level.

A central securities depository (CSD) is a financial institution, which retains securities (e.g. shares, bonds, etc.) in materialized (paper) or dematerialized (electronic) form in a manner that allows their owners to dispose of such securities (i.e. transfer them to other owners, use them as collateral in securities trading, etc.). Today, most depositories also provide services in the area of the securities transaction settlement, clearing, etc. In many countries, national securities depositories tend to be traditionally linked to stock exchanges; however, they may also exist separately.

In addition to national central securities depositories, there are also international central securities depositories. In the IOSCO classification, such depositories are referred to as the securities settlement systems – SSS. The best-known depositories are, for example, Clearstream (formerly known as Cedel), Euroclear and SIX SIS (based in Switzerland). In many countries, both national and international central securities depositories operate simultaneously.

The term central counterparty (CCP) tends to be used in a situation, where the clearing financial transactions of one party to a transaction/dealing are ensured by a single – “central” – institution. In the IOSCO concept, the role of a central counterparty does not have to be assumed by clearing institutions only. The reason for the detachment of this function as a specific component of the financial market infrastructures is the fact that a specific counterparty must now always be known for trades in securities or other financial assets (e.g. financial derivatives), so that it is absolutely clear,
which part bears the counterparty risk. Such practice stems from the experience from the period of the financial crisis, as it was not always necessary (or possible) to identify a counterparty for many financial transactions (stock exchange and off-exchange transactions). In case of a default of such unidentified or unidentifiable counterparty, the financial loss was borne by the original financial transaction bearer.

Similar reasons have also led to the creation of the central electronic transaction database – i.e. trade repositories (TR). These entities keep centralized electronic records of transactions with off-exchange (OTC) financial derivatives. The main objective for creating the centralized database of financial derivative transactions is to increase transparency of such transactions, which should contribute to limiting the noncompliance with or circumvention of stricter regulations, limit fraudulent transactions, and more effectively face financial criminality.

The concept of the financial market infrastructures from the perspective of IOSCO focuses on the systems and institutions that affect the financial market directly; the basis for this focus is the effort aimed at limiting the financial risks of entities entering the financial market.

The above mentioned classification newly classifies individual components of the financial market infrastructures; these components had previously been viewed independently, but nowadays they are viewed as a structured system. This new approach has also resulted from the problems invoked by the last global financial crisis. The new systemic approach to the financial market infrastructures means that individual FMIs have to be viewed as a structured system, i.e. individual components must be interconnected by consistent regulatory regulations and measures, differentiated for various groups of entities entering the financial market, for different financial products, as well as for different types of financial risk (counterparty risk, liquidity risk, newly systemic risks as well).

2. INTERNATIONAL ORGANISATIONS AND THE NEED OF FMIS REGULATED DEVELOPMENT

If the world FM have to be able to minimize the impacts of the next potential financial and economic crises, it is quite clear that FMIs have to be appropriately monitored, overseen, and regulated. The next paragraphs are discussing some selected problems of FMIs international regulation.

2.1 International organisations taking care of FMI internationally regulated development

At present, there are a great number of international organisations, institutions and other international bodies involved in activities connected with the international regulation of FMIs as a whole, or of their different components. As the world FM is regulated, FMIs have to be regulated as well – both at the national and the international levels.

Since the last century 80ties, the International organisation of Securities Commission (IOSCO) had a very important role in most activities on the field of FM international regulation. During the 90ties the IOSCO activities expanded and embraced the FMIs regulation as well. These activities are manifold – they include, for example, setting up the rules of trading (for different financial market segments), financial trades’ settlement, financial technical standards, ethical standards, financial conglomerates etc. They consist of, monitoring, oversight, enforcement, technical and procedural standards setting, best practices recommendations etc. To be able to perform all these activities, IOSCO has to co-operate with many other international organisations and institutions.

At present, IOSCO is a member of, participates as an observer in, or coordinates with a number of other international organizations, including: the Financial Stability Board and the Joint Forum, the International Monetary Fund and the World Bank, the International Bank for Settlements, the International Accounting Standards Board, the International Federation of Accountants, the Organization for Economic Co-operation and Development, the Financial Action Task Force on Money Laundering, the Public Interest Oversight Board, the European Commission, and many other organizations (professional organizations - such as the WFE, FESE etc. – as well.
All international organizations, institutions, boards, forums, task forces or other bodies have a common interest: to strive for better international relations between their members on different fields (as they are defined by their Statutes and other documents), and for internationally accepted rules, standards and regulations.

At a first glance, it is obvious that international organizations have different goals and tasks; most of them are interested in FMIs problems in a partial way – so far as it has a direct or indirect (or a higher or lower) importance for achievement of their main goals and tasks. In our list, they are not ranged according to homogenous criteria.

This paper does not present a deeper description and an analysis of the character of contacts between the IOSCO and the above international organisations. There are two main reasons: firstly, the situation is frequently changing: for example, some of the new task forces have a temporary character – they exist for a limited time. Secondly, the co-operation of different international bodies is not published for the public; the results of such co-operation frequently are often incorporated into final reports with a delay. To draw something as an “organization chart” of different international bodies’ co-operation is almost impossible.

To be able to understand the present state of affairs, the historical development tendencies of international economic and financial relations on the field of FM and FMIs are briefly described.

2.2 Historical development of the international co-operation

Broadly speaking, international contacts between national states’ different organisations and institutions developed in the following way: the first step was to start talks with neighbours (neighbour countries) about trading, payments, labour force movements, banking etc.; this step always is connected with information exchange which is an important pre-condition of any agreements. This is the stage of inter-state consultation; with growing numbers of partners the consultations, the information exchange will become international.

Next step is the co-operation between national states, the result of which usually is an international agreement on co-operation on different fields of mutual interest. The process of international co-operation can be characterized as the process of working or acting together for common/mutual benefit of co-operating subjects (as opposed to working in competition for selfish benefit.

In certain situations (and conditions), the closer, successful and beneficial co-operation between a number of states (and/or of different national organizations and institutions) will lead to the attempts to co-ordinate certain efforts to strengthen the existing co-operation and to multiply the effects. Co-ordination is the act of organizing, making different organizations and institutions to work together for a goal or effect to fulfill desired pre-defined goals. Co-ordination is a function in which different activities of the business are properly adjusted and interlinked. Co-ordination means a situation in which all interested subjects can realize mutual gains, but only by making mutually consistent decisions. The coordinated choice of technological, technical, economic, financial, ethical etc. standards is the striking example of what has been happening during the last decades in the world economy. At present, this trend continues, and probably will continue, if international peace will not be disturbed by broader war conflicts.

At the actual stage of the world economic development, the international co-operation on of financial markets and financial markets infrastructure development and its regulation practically represents the only way how to achieve creation of generally accepted rules and recommendations acceptable for all interested subjects. It is as stage which can be relatively stable, i.e. which allows for an agreed, reasonable level of the general financial stability. This stage corresponds to the degree of world economy internationalization. If we would analyse the development of FM and FMIs international regulation (mainly based on information exchange and a growing transparency), we
would be able to discover the main trends in different FM segments, and a similar pattern of FMI
trends in different FM segments, and a similar pattern of FMI main components.¹

Since the last 50–60 years, a new phenomenon can be observed, namely, the tendency of
integration which signalizes the general gradual, long-term trend from internationalization to
globalization of the world economy. There are examples of many attempts of integration, which are
more or less successful. The actual most advanced form of integration is the case of the European
Union. In a certain sense, this case is unique. But the experience of the EU economic and financial
integration shows that neither the economic policy co-operation, nor its co-ordination is enough to
achieve the stage of integration. A necessary pre-stage of a full integration is the policy
harmonisation. Harmonization of economic policy has to be based on harmonization of law, i.e. on
the process of establishing common laws and standards across the European Union.

The above specific types of activities represent the forms and/or methods by means of which
international relations are developed. During the process of FM and FIMs historical development,
all these methods have been applied to be able to achieve the optimum state of regulation.

2.3 Main features of FIMs regulation in 2007–2014

During the global financial crisis (mostly as a result of G7 and G20 Summits, etc.) many international
organizations actively sought stricter regulation of financial markets and, at the same time, a better
regulation of financial market infrastructures.

Compared to the situation at the beginning of this millennium, now the representatives of most
international economic organizations stress the need for improving co-operation and information
exchange. Under the pressure of impacts of the global financial and economic crisis, the situation on
the field of FIMs regulation has been improving.

The extent of regulatory measures initiated by international organizations (e.g. in connection
with the preparation and implementation of measures under the Third Basel Agreement) is
impressive. The period of the last 5 to 8 years may be viewed as a qualitative change, not only in
terms of the content of adopted measures, but also in terms of the thoroughness of their preparation,
with hundreds and thousands of financial experts from all over the world being involved. The
international economic organizations and institutions paid special attention to regulation of financial
derivatives (among others), as serious problems emerged in this area during the crisis.

3. IOSCO AND ITS ACTIVITIES RELATED TO FMI

The International Organization of Securities Commissions (IOSCO, 1983) is an association of
organizations that regulate the world’s securities and futures markets. Members are typically the
Securities Commission or the main financial regulator from each country. At present (2014), IOSCO
has 182 (109 ordinary, 11 associate, and 62 affiliate) members from over 100 different countries, who
regulate more than 90 percent of the world's securities markets (IOSCO, 2014a). IOSCO is structured
into a number of committees (IOSCO, 2014b) that meet several times per year at different locations
around the world and it has a permanent secretariat based in Madrid.

3.1 The IOSCO role

Because of the internationally recognized FM and FMI high importance, IOSCO role on this field –
since the foundation of this organization in 1983 – has been growing. The increasing volume of
securities trading was one of the reasons, why IOSCO – as one of the international organizations
which was composed of different types of members, i.e. not only of national states’ regulatory
organizations, but of SROs and international and national professional organizations and institutions
- became an international centre where many international documents were prepared, discussed and

¹ See the Final Note at the end of this paper.
agreed. What is extremely important, it was the ability of IOSCO to find reasonable solutions of many controversial proposals, initiatives and standpoints which finally were melted down in the form of useful recommendations.

Notwithstanding, it is necessary to point out that the most important decisions on the field of FM and FMIs were taken since the beginning of the new century, and especially, as a result of the world financial and economic crisis. Were it not for this crisis of catastrophic impacts, the new regulatory framework probably would not come to existence or its significance would be limited.

At the same time, it is necessary to stress that the new forms and methods of international co-operation, co-ordination and regulation which were already applied during the world crisis were of crucial importance, and they significantly contributed to the mitigation of disastrous crisis’ impacts on the international and national FM and FMIs.

What are the main elements of the new ways how IOSCO co-operates and tries to co-ordinate its efforts with the other international and national regulatory institutions and with different professional organizations and institutions? These elements, in my opinion, are the following ones: 1) the broad membership and information basis; 2) a higher transparency of information and policy decision-making; 3) the participation of educated professionals of different branches (economists, jurists, sociologists, politicians, entrepreneurs etc. the presence of whose allow for an interdisciplinary approach) and the application of team-work by inviting experts from different layers of society; 4) the use of more complex methods of organized discussions about new proposals (documents), preceding the final decision-taking process. Interested parties are invited to comment on the new draft-documents, and their comments are of a high importance; 5) a better division of labour and a higher level of co-operation (in comparison to the state of affairs before the end of last century) of different international organisations and other subjects, as far the FM and FMIs regulation is concerned, the better the results of efforts to minimise the danger of not agreed, opposing or controversial regulatory measures taken by interested parties.

One of the most efficient policy instruments applied by IOSCO is the document called “A Multilateral Memorandum of Understanding on enforcement cooperation” (MOU), through which IOSCO members pledge to provide each other with collecting information and witness statements in an enforcement investigation (IOSCO, 2002). It is an important instrument which supports the authority of IOSCO as a regulatory institution.

During the last decade, the above characteristic features of the international regulatory measures preparation have been more generally applied than ever before. In this respect, the experience of the difficult preparation of Basel III Agreement probably was the most important factor of this fact.

3.2 Principal policy public documents about FIMs

In the area of financial market infrastructures regulation, it is necessary to emphasize the complex measures associated with the new version of the Principles for financial market infrastructures of 2011, which were extensively discussed by experts (OICV-IOSCO, 2011b). In April, CPSS and IOSCO issued new standards for FIMs, including three reports which aimed at strengthening of FIMs.2

The following measures are viewed as new in financial market infrastructures regulation: a more rigorous approach to the supervision criteria, financial risk analyses and risk management (counterparty risk, liquidity risk, systemic risks and other risk forms), both from the microeconomic and (particularly) macroeconomic perspective and on the national and international level.

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2 i. e. a report on Principles of Financial Market infrastructures, a consultation paper on Assessment methodology and a consultation paper on a Disclosure framework for the standards. By the new standards (called Principles), the former sets of international standards, i.e. the Core principles for systemically important payment systems (CPSS, 2001), the Recommendations for Securities Settlement Systems (CPSS-IOSCO) and the Recommendations for central counterparties (CPSS-IOSCO, 2004) were abolished. See: http://www.iosco.org/news/pdf/IOSCONEWS230.pdf
One of the public documents issued by the Committee on Payment and Settlement Systems and the IOSCO summarizes the importance of the regulation of financial market infrastructures as follows: “Financial market infrastructures (FMIs) play an essential role in the global financial system. The disorderly failure of an FMI can lead to severe systemic disruption if it causes markets to cease to operate effectively. Accordingly, all types of FMIs should generally be subject to regimes and strategies for recovery and resolution.” (CPSS-IOSCO (2012a).

In December 2013 – to be able to evaluate the results of PFMIS application – assessment methodology for the oversight expectations applicable to critical service providers was published. Since 2011, market risks have been monitored and overviewed. According to the last IOSCO Staff Working Papers, the three main imminent risks were identified, namely: 1) regulatory uncertainty, 2) banking vulnerabilities, 3) capital flows. This analysis is based on answers of some 200 financial institutions addressed by the IOSCO; it will be used for the IOSCO Securities Market Risk Outlook (to be published late September 2014).

In July 2014, IOSCO opened the public information repository for central clearings requirements for all users (up to July, the access to the repository had the members only) (IOSCO, 2014c). A new task force composed of representatives of BCBS and IOSCO was established. It’s task is to undertake a wide-ranging survey of securitizations markets worldwide. All these activities are connected to the efforts for a more effective international FIMs regulation.

3.2.1 Some details about the IOSCO documents on FMIs

Many documents issued by IOSCO after 2007 were directly or indirectly motivated by results of a series of G-7, G-20 and other Summits which tried to coerce the impact of the world financial crisis. As a result, a closer co-operation of different international bodies was started. A new stage of cooperation aiming at anti-crisis FM regulation began.

It can be seen that the majority of documents on FMIs were issued in mutual cooperation of the Committee for Payments systems (CPSS) which is one of the most important committees of the Bank for International Settlements Committees and IOSCO. It can be seen as well that all the 5 components of the FMIs are systematically handled.

IOSCO NEWS is a useful source of information on the field of FMIs, because enables a reader to directly switch to the original Reports. In the table 1 the main regulatory measures are registered, however the above list is only a survey of the main topical decision. To get the detail information the Reports must be studied.

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4 The task-force will have to „survey securitisation markets with the aim of understanding how they are evolving in different parts of the world; identify factors that may be hindering the development of sustainable securitisation markets; assess whether there are factors inhibiting the participation of investors, particularly non-bank investors; and develop criteria to identify and assist in the development of simple and transparent securitisation structures. The task-force was established in consultation with IAIS and IASB. See: BCBS-IOSCO.(2014). BCBS-IOSCO Task Force conducts a survey on securitisation. http://www.iosco.org/news/pdf/IOSCONEWS337.pdf
### Tab. 1. IOSCO News on the issuance of documents directly related to FMIs (2009–2014)

<table>
<thead>
<tr>
<th>Year</th>
<th>Content of Documents <em>(abbreviated)</em></th>
<th>Date</th>
<th>Issued by</th>
<th>No.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>• Recommendations to Central Counterparties</td>
<td>20.7.</td>
<td>CPSS/IOSCO</td>
<td>1</td>
</tr>
</tbody>
</table>
| 2010 | • Standards for Payment System  
       • Guidance for CC and TR | 2.2.  | IOSCO/CPSS CPSS/IOSCO | 2   |
| 2011 | • Principals for FMIs | 10.3. | IOSCO | 1   |
| 2012 | • OTC Derivatives Clearing  
       • New Standards for FMIs  
       • Consultative Report on FMIs Recovery and Resolution  
       • Consultative Report on FMIs Recovery and Resolution  
       • Assessment Methodology for FMIs | 29.2.  
       16.3.  
       16.4.  
       31.7.  
       14.12 | IOSCO CPSS/IOSCO CPSS/IOSCO CPSS/IOSCO CPSS/IOSCO | 5   |
| 2013 | • Comments on Rep. on Recovery and Resolution  
       • Authorities’ Access to TR Data  
       • Implementation of PFMIs  
       • Authorities’ Access to TR Data  
       • Report on Principles’ Implementation  
       • Report on FMIs Recovery and Resolution  
       • Consultative document On Quantitative Discloser by CC  
       • Responses to Consultations on FMIs Recovery | 18.1.  
       11.4.  
       17.4.  
       12.8.  
       12.8.  
       12.8.  
       15.10.  
       8.11. | IOSCO CPSS/IOSCO CPSS/IOSCO CPSS/IOSCO CPSS/IOSCO CPSS/IOSCO CPSS/IOSCO | 8   |
| 2014 | • Responses On Quantitative Discloser by CC  
       • Monitoring for the PFMIs  
       • Public Information on the Repository for CC Requirements | 7.2.  
       28.5.  
       5.8. | CPSS/IOSCO IOSCO IOSCO | 3   |

Source: author’s table is based on IOSCONEWS

### 3.2.2 IOSCO co-operation with IFRS

During the period of 2008–2014, the main co-operation between the IOSCO and IFRS has been implemented in the form of “Comment letters” which were addressed by IOSCO to six IFRS organizations. These letters commented on different IFRS Consultative documents; critical remarks, objections and amendments were discussed and material, technical and procedural proposals were passed to the addressees.

As an example of the wide extent of this form co-operation the number of the IOSCO comment letter addressed to the IASB was more than 60 (period 2007–2013).

In 2014, a cross-sectoral Task Force on Securitisation Markets was set up; it will be co-led by the BCBS and IOSCO. The new Task Force was established in consultation with the International Association of Insurance Supervisors (IAIS) and the International Accounting Standards Board (IASB).

To conclude: the extent of regulatory problems studied by IOSCO, in fact, is broader than it corresponds to the above IOSCO narrower definition of FIMs. IOSCO, for example, is involved in problems of rating, auditing, accounting, corporate financial disclosure, financial information transparency, reporting, monitoring etc. etc. For this reason, *inter alia*, not only a close co-operation, but a co-ordination of interested organizations activities on the field of FT and FMIs regulation would be most desirable.
CONCLUSION

At present, the crucial problem of FMIs regulation is the problem of financial stability: FMIs have to contribute to FM financial stability. The application of FIMs Principles is one of the tools how this difficult task can be implemented.

To-day, on the top of the international organisations and institutions responsible for the world financial stability formally is the Financial Stability Board; however, the main decisions paving the way for a more efficient financial regulation at the international level are taken by the G-Summits.

The FIMs regulation is only one relatively small part of the world international regulatory problems. Therefore, on one side the IOSCO activities on the field of FMIs are subordinated to the whole system of world-wide measures; on the other side, IOSCO is involved in many other regulatory tasks which were not discussed in the paper.

BIBLIOGRAPHY


Final Note

The paper has been prepared as part of a project financed by the funds for specific university research. Project name: Regulation of the financial market infrastructure – goals, possibilities, and potential impact – Vysoká škola finanční a správní, o.p.s. (University of Finance and Administration). Project number: 7427.
INCURRED LOSSES vs. EXPECTED LOSSES: A CRITICAL COMPARISON

Helmut SILLER
Dr. Helmut Siller Betriebsberatung und Training
Siller@Beeratung.net

Pietro Andrea PODDA
Anglo-American University
Pietro.Podda@aauni.edu

Abstract: Our paper discusses critically two models which can be used to measure credit losses: ILM and ELM. So far, International Accounting (IAS 39) was oriented towards the ILM. This method is based on the assumption that loans will be repaid, unless there is evidence which strongly suggest the opposite. Only in case there is clear indication that a loan will not be repaid, the reporter has to write down the asset to a lower value. This method leaves a certain margin of optimism, as diminution of value does not have to be recognized even when a loss is reasonably probable. However, there is another method, called ELM, which has been endorsed by IFRS 9. The International Accounting Standard Board (IASB) and the US Financial Accounting Standard Board (FASB) are cooperating in order to refine the prescriptions associated with IFRS 9. According to this seemingly innovative model, the value of a financial asset can be written down when a loss is expected, without the need to wait until the loss itself materializes. Background is to foster the idea of early recognition and to provide a more realistic presentation of those financial assets which should be measured according to the ELM. Our paper discusses critically advantages and disadvantages of both models and formulates recommendations.

Keywords: IFRS, IAS, IASB, Incurred Cost Model, Expected Cost-Model

INTRODUCTION

This paper discusses the two main methods used to estimate future credit losses: ILM (ILM) and ELM (ELM). The issue appears of importance because of the planned introduction of IFRS 9 and the consequent shift from ILM ILM (prescribed by IAS 39) to ELM as measurement of impairment of credits. Both methods have advantages as well as shortcomings, hence an analysis appears important in a moment when accountants and analysts are expected to develop familiarity with another mechanism for estimating credit losses.

Technically, a loss means that the carrying amount of the credit exceeds the present value of the future cash-flows. Such an occurrence may arise for various reasons, for example when the debtor has problems in repaying due debts, or the rating of the debtor decreases, or when the debt should be set using the currency of the debtor, this currency depreciates and there is no hedging from the side of the creditor. Hence, these losses can be expensed with a consequent impact on the Income Statement and subsequently on the Balance Sheet. The rules for recognizing a loss have an impact on the financial statements and financial reporting. As for the Balance Sheet, the value of assets (like e.g. receivables, held debt instruments) results to be impaired in presence of a loss.

The aim of this paper is to enhance awareness of the characteristics of both methods of evaluation and of the likely consequences that the abandonment of the ILM and the introduction of the ELM can have. Our strategy is to accompany the presentation of the technical aspects of the whole matter with a qualitative and substantial analysis of the general meaning and possible consequences of changing the patterns and methods of evaluating/recognizing financial items. Our main point is that there cannot be perfectly effective systems and probably not even superior or necessarily more
effective methods for recognizing/measuring debt collection risks. The choice of the rules depends
often on the strength of specific lobbying groups and, as in this case, it can be a reaction against the
weight that the downsides of the previously prescribed method have had as co-determinants of –
specific financial scandals or of a major financial crisis. In our case, the limitations embedded in the
ILM have led to an under-statement of the specific risks that banks were running as for the quality of
loans.

Our paper is structured in the following way. The first section will describe the ILM, the
second one will present the ELM. A third section will compare the two methods critically. References
will follow.

1. AN OVERVIEW OF THE INCURRED COST MODEL (ILM)

The ILM is a method for evaluating credit losses and has been prescribed by International Accounting
Standards (IAS 39) since 1998. The steps and the rationale that led to its introduction have been
reconstructed by Camffeman (2013). As usual, there has been a long process which has led to the
introduction of a particular rule by the IASB and also by its American counterpart, the FASB (Baskin,
1992). The idea to prescribe the use of ILM was motivated by the need for banks to maintain profit
level as the ILM allows, recording of a loss is possible only in presence of a particular event which
indicates that the loss has actually been incurred and has materialized. This principle has various
consequences, among the most important ones is that reporting companies cannot expense non-
incurred but (highly) probable losses. Hence, reporting companies were deprived of the option to
reduce the amount of profits and therefore save taxes, a possibility that various banks had hitherto
exploited.

IAS 39 prescribes that at each balance sheet date, financial assets or groups of financial assets
representing credits must be tested for objective evidence of impairment (IAS 39.58 and .59). This
type of assets must be tested individually when they are individually significant, otherwise the whole
portfolio is tested. No Bad Debt provisions are allowed at initial recognition (day one). Impairment
may be recognised in the presence of objective evidence which has arisen after issuance. Impairment
loss, as the difference between carrying amount and present value of the estimated future cash flow,
is measured on the basis of the original effective interest rate. Still, according to the rules of the
Standard, financial assets (representing credits) are grouped on the basis of similar credit risk
characteristics (IAS 39.AG87) and allowances for collective (portfolio) impairment on a performing
portfolio is allowed only for incurred (even if not yet reported) losses. Expected losses are not
recognised before trigger events occur.

Main characteristic of the ILM, as said, is to make the recognition of the loss dependent on
an occurred fact. Therefore, the ILM appeared as a way to constrain banks (among other companies)
to refrain from manipulating their costs with the relevant consequence to save on both taxes as well
as to reduce the basis for payment of dividends. Reporting companies should wait for a material event
to occur before recognizing a loss. This type of events entails a reduction of the amount of money
that the creditor may reasonably expect to receive and are therefore classifiable as a loss on the credit.
Advantage of the method is that a loss can be recognized only when there has been an event which
has led to a loss of value of the credit (in case this latter carried a commercial value) or to a reduction
of the probabilities to recoup the contractually-embedded sum. This means that recouping companies
cannot artificially record a loss irrespective of a supposedly objective reason underpinning the
recognition. On the other side, there is also a disadvantage associated with this particular method.
This lies in the fact that, especially when there is a portfolio of assets representing credits, a certain
amount of losses is highly probable on the basis of experience and on the basis of the likely evolution
of financial markets or a debtor’s repayment records. Sometimes a loss, despite being reasonably
expected, cannot be recognized in P&L with the result that financial statements appear (much) rosier
than they really are. Thus, financial statements fail to reproduce a realistic picture of the real state of
the company. This type of problem has been witnessed at the time of the financial crisis of 2007–
2010, where financial statements of banks continued to report credits at their full value, even when the credit-worthiness of the debtor was clearly doubtful.

The application of the ILM has allowed earnings management, i.e. banks were able to postpone losses and to hide the risks that certain financial instruments were generating inside the reporting entity. The truth came to be known only when the loss was actually incurred and affected stakeholders heavily and suddenly, without giving them any chance to react. Delayed loss recognitions generated a cyclical effect, and interest revenues were over-stated.

2. AN OVERVIEW OF THE EXPECTED COST MODEL (ELM)

The IASB was heavily criticized during financial crisis for allowing the loss recognition only after devaluation had already materialized thus fostering procyclical effects and also for the ILM’s alleged complexity. Since 2009 the Board has been working on redrafting loss recognition rules (Boochs, 2013).

In 2009 the IASB made the first proposal (ED/2009/12), i.e. calculating bad debt losses by applying the financial instrument’s effective interest rate. Basic idea was to take into account the expected credit losses in interest income.

This proposal was welcomed by a majority of addressees as conceptually convincing, but finally rejected owing to the fact that banks in their operating business only in rare cases checked the valuation of the financial instrument’s creditworthiness.

As supplement in 2011 IASB and FASB suggested a model in which interest recognition and recognizing bad debts was uncoupled again (ED/2011/1). Following that supplement financial instruments should have been divided into a white and black book, whereby

- in the white book all financial assets shall be attributed where no default is likely, whereas
- all other credits should go into a so-called black book (comparable to a “bad bank”).

While bad debt credit losses in the black book should cover the credit’s remaining duration – which roughly corresponds to the bad debt recognized under the ILM – risk provision for the business cases documented in the white book shall reflect expected credit losses during the credit term. In case a default becomes likely bad debt should be increased.

In March, 2013, IASB presented a third proposal (ED/ 2013/3) which suggests to build risk provisions also for hitherto non-performing financial instruments.

On July 24, 2014, the IASB completed the final element of its comprehensive response to the financial crisis by publishing IFRS 9 (Financial Instruments). The improvements introduced by IFRS 9 include a model for classification and measurement, ELM and a substantially-reformed approach to hedge accounting. IFRS 9 will be effective for annual periods beginning on or after 1 January 2018. The ELM will require a more timely recognition of expected credit losses. Specifically, the new Standard requires entities to account for expected credit losses when financial instruments are first recognised and to recognise full lifetime expected losses on a more timely basis. The IASB has already announced its intention to create a transition resource group to support stakeholders in applying the new impairment requirements (Agnew, 2014).

In the ELM it is no longer required to have a trigger event. So more timely information is required about expected credit losses. IFRS requires an entity to base its measurement of expected credit losses on reasonable and supportable information that is available without undue cost or effort and that includes historical records and forecast information (IASB, 2014).

IFRS 9 applies on impairment model to all financial instruments: those classified as amortised cost and FVOCI, lease receivables, trade receivables, commitments to lend money and financial guarantee contracts.

Credit losses are the present value of all cash shortfalls. Expected credit losses are an estimate of credit losses over the financial instrument’s useful life. When measuring an expected credit loss (i.e. cash shortfall), an entity should consider the probability-weighted outcome, i.e. an estimate that reflects the variant that a credit loss occurs and the variant that no loss occurs, further the time value
of money, i.e. the expected credit losses should be discounted to the reporting date, and reasonable information that supports that calculation.

The ELM comprises a three-stage-approach as follows:

Stage 1: As soon as a financial instrument is originated or purchased, a 12-month expected credit loss is recognized in P&L and a loss allowance is made. For financial assets, interest revenue is calculated on the gross carrying amount (i.e. without adjustments). Hereby 12-month expected credit losses are the portion of the lifetime expected credit losses associated with a possible default within the coming twelve months.

Stage 2: In case credit risk increases significantly and the resulting credit quality worsens, full lifetime expected credit losses are recognized. The interest revenue calculation is the same as in stage 1. Hereby lifetime credit losses are an expected present value measure of losses that arise if a borrower defaults on his obligation during the term.

Stage 3: When on individually assessing financial assets a financial asset’s credit risk rises further and to a point that is considered credit-impaired, interest revenue is calculated based on the amortised cost (i.e. gross carrying amount adjusted for the loss allowance).

IFRS 9 marks a big change for banks, insurance companies and every user of financial statements. These entities will have to recognize not only credit losses that have already occurred but also losses that are expected in the future. That shall help to ensure that they are appropriately capitalised for the loans that they have created.

The IFRS 9 publication comes as the largest banks across the Eurozone are facing the ECB’s stress tests and asset quality review in November 2014, which could result in higher loan loss provisions.

Efforts between the IASB and the FASB to create a coordinated financial instruments standard ended in early 2014 without result, thus reducing the comparability of European financial institutions against their US counterparts.

3. A CRITICAL COMPARISON

The description offered above about the two different methods suggests that the tricky point is to establish the rules for the recognition of a loss. The literature suggests that in principle there is a continuum of choices between two extreme methods: recognizing the loss only after it has undeniably occurred and recognizing a provision whenever a loss is reasonably expected.

All forms present advantages and disadvantages which are specular. The ICM has the advantage of linking the recognition of a loss to an “objective” occurred fact, a real circumstance, thus preventing opportunistic recognition of losses based only on the need to save on taxes and dividend distribution through the shrinking of Profits. This strategy has been followed by certain companies in the past and had led to the introduction of more stringent criteria for the recognition of a credit loss, criteria embedded in the ICM. On the other side, the recognition of a probable loss is delayed until it actually occurs. Recurring to a metaphor, this situation reminds of the case of the man falling down from a high building and declaring to feel well before crashing on the soil. The Financial Statements risk giving an over-optimistic representation of the financial position of the company, understating a probable impairment of a credit. This means that the principle of Prudence (or Vorsicht), central to Central European Accounting, is fundamentally violated.

On the other side, the ECM allows to rectify to the shortcoming of the ICM. On the other side, despite all possible mechanisms of prevention, it still makes the recognition of a loss depending on subjective factors or, at best, on previous experiences. This fact may represent a threat to the respect of the principle of Reliability and entail also opportunistic recognitions, as already outlined.

The tricky point is to establish the rules for the recognition of a loss. As often, it is hard, and probably impossible, to conclude for the superiority of one model in comparison with another one. This represents a constant characteristic of various set of alternative ways of regulating the
representation of financial data. Examples are Fair Value vs. Historic Cost Method, Independent vs. Government-controlled Central Banks, Auditing Companies restricted from offering additional services to clients vs. Auditing Companies offering various services. In these and other similar cases, there are alternative ways of regulating financial activities, all of them carry advantages and shortcomings. There is not an alternative which can necessarily be considered as the best one.

Indeed, the choice depends on the actual context, on the challenges that the sectors involved are facing at any particular time and on the strength of specific lobbying groups. There are moments when the current situations may suggest to give priority to certain factors rather than others. For example, the independence of the Italian Central Bank from the Government finds its roots in the scandals which accompanied various banks in the late 19th century. In our case, the shift to the ECM is due also to the weight that over-optimistic representations of the financial positions of various banks have had as for the emergence of the last financial crisis.

Our final message is that the ECM will allow to rectify the shortcomings of the previous model but is not and cannot be a perfect option.

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Abstract: At the end of the accounting period all statutory audited business entities have to prepare and submit to the business register the annual report – the on-time submission of the financial statements is of a high importance for all stakeholders to be able to make proper economical decisions. This paper represents the examination of whether the implementation of the e-submissions of financial statements has influenced the on-time submission by the selected companies. In order to determine whether e-system influenced positively the on-time submission of annual reports authors have selected the annual reports submitted to the Czech Business Register by the most successful TOP100 Czech companies in the period 2007–2012. The results revealed that Czech companies are still not very willing to submit their financial statements on time.

Keywords: Financial reporting, Presentation, TOP100, European Union, Czech Republic

1. INTRODUCTION

Many researchers have focused their studies on the accounting mandatory disclosure (Abu-Nassar and Rutherford, 1996; Arnold and Moizer, 1984; Firth, 1979; Lee and Tweedie, 1975) mainly because of the exactly specified regulations that provide the content, the format of information and the variety of the data included in the financial statements.

On the other hand significant group of researchers have focused their studies on accounting voluntary disclosure because the disclosure of other corporate reports in addition to the minimum requirements, could reduce information asymmetry and agency conflicts between managers and outside investors (Healy and Palepu, 2001; Lambert et al., 2007; McNally et al., 1982). Healy and Palepu (2001) analyze managers’ reporting and disclosure decisions in a capital markets setting. They believe that six forces affect managers’ disclosure decisions for capital market reasons as follows: (i) capital market transactions, (ii) corporate control contests, (iii) stock compensation, (iv) litigation, (v) proprietary costs, and (vi) management talent signalling.

The link between corporate disclosure policy and analyst behaviour has also been investigated (Lang and Lundholm, 1996) as well as the relationship between disclosure level and the cost of equity capital (Botosan, 1997; Botosan and Plumlee, 2002).

By investigating the annual reports for 2001 of 100 French firms belonging to the SBF 120 stock index, Chavent et al. (2006) found that the disclosure pattern is associated with provision intensity, size, leverage and market expectation. Companies with the highest score for disclosures have the greatest provision intensity, firm size, leverage and market expectation.

Timeliness of financial reporting is also considered to be the part of the fundamental financial accounting qualities. However, the on-time submission of financial reports varies from country to country depending on various factors. Numerous studies show mixed results in regards to the factors, which influence timeliness of submission the annual reports. Basu (1997) and Haw et al. (2000) reveal that timeliness is directly related to the net profit earned by the company. The higher the profit, the more quickly one can expect the annual report to become publicly available. Based on the information of listed Chinese firms with A-shares for 1994-1997, Haw et al. (2000) found that companies are willing to report good news, prepare and submit their annual reports earlier than companies with bad news, and companies with financial loss release their annual reports the latest. This is also confirmed by the findings of Han and Wild (1997) showing that the timing of earnings reports has significant
and far-reaching economic consequences. In their study they found that earlier earnings releases yield negative information transfers, earnings releases yield negative (nominal) information transfers to firms that previously (subsequently) release their earnings reports, and earlier earnings releases yield negative information transfers to firms that have not yet disclosed earning. (Han and Wild, 1997).

There is also an opinion that the economic decline has significantly influenced the timeliness of financial reporting making the situation worse and that the various measures implemented by different countries, like new government regulations, reporting systems etc., have made a positive impact on the on-time submission of annual reports. This opinion is supported by the studies of Vichitsarawong et al. (2010), of the impact of the Asian financial crisis on conservatism and timeliness of earnings. Their studies revealed that timeliness of earnings during the crisis period were low, but improved in the post-crisis period. The results of their studies also indicated that the introduction of the corporate governance measures to stabilize financial systems and improve regulation in the four selected Asian countries had the positive impact on the conservatism and timeliness of earnings. The studies of Lai et al. (2013) examined the impact of mandatory International Financial Reporting Standards (IFRS) adoption on accounting conservatism in Australia. Evidence suggests the adoption of IFRS has led to a decrease in conditional conservatism (i.e. asymmetric timeliness).

2. METHODOLOGY

As living currently in information society, on time data are vital for current creditors as well as for potential investors. From this perspective we did surveyed whether reputed TOP100 companies in selected countries are willing to publicly present their data.

For our analysis we opted for two countries from CEE region that entered European Union in 2004, concretely Czech Republic, being one of the leading economies from the new block EU countries. Data used within analysis were picked-up from publicly presented information in Business Register.

Based on current Czech accounting legislature all statutory audited companies shall present their financial reports within Business Register within the period of 30 days after their approval by company’s general assembly. Companies are submitting their financial reports in electronic form. Based on the Accounting Act all companies failing this obligation have to pay a penalty up to 3% of assets total. However there shall be stated that this penalty is obviously not applied in practice.

For this survey we did use the information about most successful TOP100 Czech companies as stated in public ranking and analyzed their on-time submission for the period 2007–2011. Firstly we did checked if these reports were submitted before the stated due date in each year and then counted the number of months since the final date of submission till the submitted date in order to find out the duration of the delay period.

3. RESULTS AND DISCUSSION

There were used the information base of the Czech Business Register (www.justice.cz), accessed in June–July 2013 and have got the information about the approximately 500 reports of the 92 companies. From those companies significant number use as an accounting period not a calendar year, that’s why the end of the accounting period fell onto consequent year.

For the year 2007 we were able to use the annual reports of only 85 companies as some companies were established during this period or later and for some companies no reports were found in the database. For year 2011 we could use the reports of 91 companies for the present research. This breakout is illustrated in Table 1.
Tab. 1. Reports used for the survey for year 2007–2011

<table>
<thead>
<tr>
<th>Year when the report was submitted</th>
<th>Number of reports used in the present survey</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>85</td>
</tr>
<tr>
<td>2008</td>
<td>86</td>
</tr>
<tr>
<td>2009</td>
<td>90</td>
</tr>
<tr>
<td>2010</td>
<td>92</td>
</tr>
<tr>
<td>2011</td>
<td>91</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>444</strong></td>
</tr>
</tbody>
</table>

Source: author’s construction based on data retrievable from Czech Business Register (www.justice.cz)

Approximately we were able to analyze around 90 companies within approached period 2007–2011. Table 2 illustrates the percentage of the annual reports submitted on time (i.e. within 30 days after approval by general assembly) and with delay. The smallest percentage of the on time submitted reports occurred in 2011 (8.8% or 8 reports from the total of 91), and the highest percentage of on time submission was reached in 2009 (13.3% or 12 reports from the total of 90).

Tab. 2. Submission of Annual Reports during Years 2007–2011 by Czech TOP 100 companies

<table>
<thead>
<tr>
<th>Year</th>
<th>On Time Submission</th>
<th>Delayed Submission</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>8</td>
<td>77</td>
<td>85</td>
</tr>
<tr>
<td>2008</td>
<td>11</td>
<td>75</td>
<td>86</td>
</tr>
<tr>
<td>2009</td>
<td>12</td>
<td>78</td>
<td>90</td>
</tr>
<tr>
<td>2010</td>
<td>10</td>
<td>82</td>
<td>92</td>
</tr>
<tr>
<td>2011</td>
<td>8</td>
<td>83</td>
<td>91</td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td><strong>11.0%</strong></td>
<td><strong>89.0%</strong></td>
<td><strong>x</strong></td>
</tr>
</tbody>
</table>

Source: author’s construction based on data retrievable from Czech Business Register (www.justice.cz)

We also found out that the structure of the delayed submissions has not been changed significantly. There shall be stated that around 80% of delayed reports is delivered within the period of 6 months after required submission date (and 45% even within the period of 3 months). The breakdown is illustrated by the Table 3.

Tab. 3. Delayed Submission of Annual Reports during Years 2007–2011 by Czech TOP 100 companies

<table>
<thead>
<tr>
<th>Year</th>
<th>&lt; 1</th>
<th>1–3</th>
<th>3–6</th>
<th>6–12</th>
<th>&gt; 12</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>20</td>
<td>19</td>
<td>31</td>
<td>6</td>
<td>1</td>
<td>77</td>
</tr>
<tr>
<td>2008</td>
<td>9</td>
<td>21</td>
<td>24</td>
<td>19</td>
<td>2</td>
<td>75</td>
</tr>
<tr>
<td>2009</td>
<td>9</td>
<td>19</td>
<td>38</td>
<td>9</td>
<td>3</td>
<td>78</td>
</tr>
<tr>
<td>2010</td>
<td>15</td>
<td>23</td>
<td>28</td>
<td>14</td>
<td>2</td>
<td>82</td>
</tr>
<tr>
<td>2011</td>
<td>13</td>
<td>25</td>
<td>31</td>
<td>13</td>
<td>1</td>
<td>83</td>
</tr>
</tbody>
</table>

Source: author’s construction based on data retrievable from Czech Business Register (www.justice.cz)

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4. CONCLUSIONS

Results show that majority of Czech TOP100 companies are willing to publicly present their financial reports, however with significant delay. The percentage of on-time submission obviously didn’t reach the result of more than 10%. Majority of delayed reports (around 80%) are submitted within the period of 6 months after deadline.

The implementation of the e-reporting system in Estonia has positively influenced the timeliness of the submission of the annual financial reports by rising the percentage of the reports submitted on time and shortening the delay period. It is also obvious that the new e-reporting system enabled companies to submit their annual report in a very easy and effective way requiring less time and efforts.

When linking the results of the survey approached in Czech Republic and Estonia, it shall be stated that the results varies only on first sight, as majority of Estonian companies fulfil their obligation on time (meaning 6 months after the end of accounting period). As the Czech legislature requires submitting the reports within one month after the approval by general assembly (obviously taking place around February/March of consequent year) there shall be stated that reports delayed for up to six months are technically in line with the Estonian deadline.

Authors suggest that the future research shall focus on investigation of the various factors of delay in submitting the reports. Such research would be relevant and useful as most companies in Czech Republic and Estonia are small and medium-sized and this study may reveal problems related to preparation and submission of annual reports and suggest further measures to improve the situation.

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Summary and Final Comments

Following the last year's successful conference “IFRS – Global Rules and Local Use” the second year was organized under the same name in 2014. Our the desire was to bring together experts in accounting theory and practice and share the creative environment with academic and student community to enable them to exchange ideas 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 characterize the current state of knowledge about application of IFRS at different levels and from different points of view. Furthermore the conference hosted papers related to new directions stemming from ethical issues and environmental accounting.

In summary, these contributions provided 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 conference contributions will bring some more inspiration for further research and for solution of actual practical problems.

The editors
List of Authors

David ALEXANDER  University of Birmingham  d.j.a.alexander@bham.ac.uk
Paul ANDRÉ  ESSEC Business School, Editor Accounting in Europe  andre@essec.fr
Diana E. BALACIU  University of Oradea  dianabalaciu@yahoo.com
Kinga BAUER  Cracow University of Economics  kinga.bauer@uek.krakow.pl
Lucie CVIKLOVÁ  Charles University, Prague  lucie.cviklova@yahoo.com
Lucian CERNUȘCA  Aurel Vlaicu University of Arad  luciancernusca@gmail.com
Mădălina DUMITRU  Bucharest University of Economic Studies  madidumitru2007@gmail.com
Valentin F. DUMITRU  Bucharest University of Economic Studies  Valentin.Dumitru@cig.ase.ro
Ionelia-Alexandra FELDIOREANU  Bucharest University of Economic Studies  alexandrafeldioreanu@yahoo.com
Vasile GORGAN  Bucharest University of Economic Studies  vasile.gorgan@cig.ase.ro
Irena JINDRICHOVSKÁ  Anglo-American University  irena.jindrichovska@seznam.cz
Gabriel JINGA  Bucharest University of Economic Studies  Gabriel.Jinga@cig.ase.ro
Zuzana JUHÁSZOVÁ  University of Economics in Bratislava  zuzana.juhaszova@euba.sk
Karol Marek KLIMCZAK  Kozminski University  kmklim@kozminski.edu.pl
Sarka KOCMANOVA  University of Finance and Administration  sarka.kocmanova@centrum.cz
Joanna KRASODOMSKA  Cracow University of Economics  joanna.krasodomska@uek.krakow.pl
Dana KUBICKOVA  University of Finance and Administration  dana.kubickova@centrum.cz
Peter MARKOVIĆ  University of Economics in Bratislava  peter.markovic@euba.sk
Ema MAȘCA  Petru Maior University of Tîrgu Mureș  ema.masca@ea.upm.ro
Ramona NEAG  Bucharest University of Economic Studies  ruxandra.mateescu@yahoo.com
Gabriele MEISSNER  Anglo-American University  gabriele.meissner@aauni.edu
<table>
<thead>
<tr>
<th>Name</th>
<th>Institution</th>
<th>Email</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ioana Teodora MEŞTER</td>
<td>University of Oradea</td>
<td><a href="mailto:ioana.teodora.mester@gmail.com">ioana.teodora.mester@gmail.com</a></td>
</tr>
<tr>
<td>Daša MOKOŠOVÁ</td>
<td>University of Economics in Bratislava</td>
<td><a href="mailto:dasa.mokosova@euba.sk">dasa.mokosova@euba.sk</a></td>
</tr>
<tr>
<td>David John MUIR</td>
<td>Anglo-American University</td>
<td><a href="mailto:david.muir@aauni.edu">david.muir@aauni.edu</a></td>
</tr>
<tr>
<td>Elena Mirela NICHITA</td>
<td>Bucharest University of Economic Studies</td>
<td><a href="mailto:mirela.nichita@cig.ase.ro">mirela.nichita@cig.ase.ro</a></td>
</tr>
<tr>
<td>Irina-Doina PĂŞCAN</td>
<td>Petru Maior University of Tg. Mureș</td>
<td><a href="mailto:pascanirina@yahoo.com">pascanirina@yahoo.com</a></td>
</tr>
<tr>
<td>Vladislav PAVLAT</td>
<td>University of Finance and Administration</td>
<td><a href="mailto:vladislav.pavlat@vsfs.cz">vladislav.pavlat@vsfs.cz</a></td>
</tr>
<tr>
<td>Anna Marta PIKOS</td>
<td>Kozminski University</td>
<td><a href="mailto:apikos@kozminski.edu.pl">apikos@kozminski.edu.pl</a></td>
</tr>
<tr>
<td>Pietro Andrea PODDA</td>
<td>Anglo-American University</td>
<td><a href="mailto:Pietro.Podda@aauni.edu">Pietro.Podda@aauni.edu</a></td>
</tr>
<tr>
<td>Helmut SILLER</td>
<td>Dr. Helmut Siller Betriebsberatung und Training</td>
<td><a href="mailto:Siller@Beeratung.net">Siller@Beeratung.net</a></td>
</tr>
<tr>
<td>Martin SKACELIK</td>
<td>EY Česká republika</td>
<td><a href="mailto:Martin.Skacelik@cz.ey.com">Martin.Skacelik@cz.ey.com</a></td>
</tr>
<tr>
<td>Donna STREET</td>
<td>Dayton University, USA</td>
<td><a href="mailto:dstreet1@udayton.edu">dstreet1@udayton.edu</a></td>
</tr>
<tr>
<td>Jiří STROUHAL</td>
<td>University of Economics Prague</td>
<td><a href="mailto:strouhal@vse.cz">strouhal@vse.cz</a></td>
</tr>
<tr>
<td>Joanna TOBOREK-MAZUR</td>
<td>Cracow University of Economics</td>
<td>to <a href="mailto:borekJ@uek.krakow.pl">borekJ@uek.krakow.pl</a></td>
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IFRS: GLOBAL RULES & LOCAL USE

Editors:

doc. Ing. Irena Jindřichovská, CSc., Anglo-American University, Prague
Ing. Dana Kubičková, CSc., University of Finance and Administration, Prague

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