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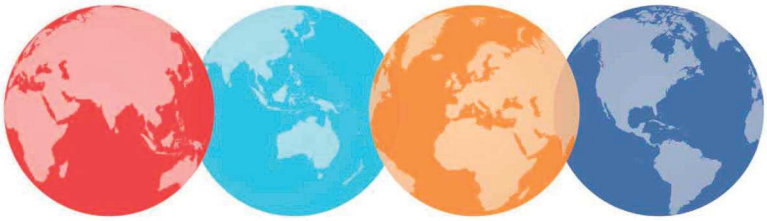

IFRS:
GLOBAL RULES & LOCAL USE

Prague, October 8–9, 2015

Anglo-American University, Prague – Czech Republic

PROCEEDINGS OF THE 3rd INTERNATIONAL SCIENTIFIC CONFERENCE

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ISBN 978-80-260-8675-8 (CD-ROM)

ISBN 978-80-260-8676-5 (on-line)

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IMPACT OF ACCOUNTING STANDARDS ON THE RESULTS OF FINANCIAL ANALYSIS

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Abstract
The current globalization trends in investment and financing mean that requirements for accounting and reporting are continuously rising, particularly in terms of comparability of financial information. The basis for the calculation of indicators of financial analysis are information from accounting, respectively from the financial statements. Their reliability and relevance largely influence the results of various financial models. The aim of this paper is to illustrate how changes in accounting rules affect the results of the financial analysis. Paper highlights the distortion, if changes in accounting rules are not taken into account in the calculation of indicators of financial analysis.

Key words: *financial statements, financial analysis, Altman Z-score, IFRS*

1. INTRODUCTION

Accounting entities in Slovakia prepare financial statements according Slovak legislation or IFRS. These accounting frameworks have their pluses and minuses. Regarding financial analysis models the results of financial analysis for the same year and the same period are radically different. The main differences in accounting frameworks are already harmonized but the transfer from Slovak legislation to IFRS can significantly influence financial ratios. Šlosárová A., Silná R. (2008). Both frameworks have their pluses and minuses. Itis not possible to consider one of these two frameworks as a universal efficient solution. This paper will attempt to describe how changes in accounting rules affect the results of financial analysis models and what constraints to consider before applying it in a company.

The changing of accounting framework can influence information presented in financial statements. Changing to IFRS allows companies to use advantages resulting from using of IFRS – for example acceptation of financial statements by investors at stock exchange. Some companies can voluntarily change accounting framework to IFRS, for others it is compulsory. It is done voluntarily in companies that are parts of international consolidated groups of companies. IFRS ensure, that financial statements are comparable within the group of companies and with competitors. Surový, V. (2010) Shareholders and other stakeholders can compare financial statements of various companies. Companies that do not provide comparable data are discriminated when acquisition of new resources and increasing of company value is limited. **Ondrušová, L.** (2011) Financial statements prepared according IFRS can be considerably different from financial statements prepared according Slovak legislation. The biggest differences are legislation dealing with financial instruments, business combinations, leasing and others. Parajka, B. (2011).

Tumpach, M. (2006) presented how the choice of the accounting method is directly related to the provision of a true and fair view of the entity, which provides the accounting and it is also indicated in the financial result. Changing of accounting framework can be also way of misstatement, misclassification as well as misrepresentation of financial analysis ratios. In essence,

description or disclosure of accounting data in order to distort the true financial picture of the organization in question. (Tumpach, M. - Užík, J. - Juhászová, Z., 2014).

Study on impact of IFRS Adoption on Key Financial Ratios published by Jindřichovská I., Kubíčková D. (2012) showed that the transition to the IFRS system impacts on the value of key financial ratios and thus influences the assessment of the financial situation and firms however it was not proved that these differences are statistically significant.

The another study performed by Kubíčková D., Jindřichovská I. (2013) confirmed that the compilation of the financial statements according the IFRS brings changes to the assessment and prediction of financial situation of firms in comparison with the Czech accounting standards. The difference can be seen in different concept and way of reporting of retained earnings and by a scope of the different reporting procedures that were reflected in both sales and assets.

2. METHODOLOGY

The purpose of financial analysis is to examine financial situation and explain processes that affect it. There are many financial analysis ratios and models that can be used. Almost all computer-assisted financial analysis have a command for Altman Z-score.

$$\mathbf{Z_o = 0{,}717 * x_1 + 0{,}847 * x_2 + 3{,}107 * x_3 + 0{,}420 * x_4 + 0{,}998 * x_5}$$

Where x_1 = Net Working Capital / Total Assets
x_2= Retained Earnings / Total Assets
x_3 = EBIT / Total Assets
x_4 = Equity / Total Liabilities
x_5 = Sales / Total Assets

Interpretation of the value of Z-score is divided into three levels according to value Z-score:
1) Values higher than 2.7 – the firm is in good condition, there is not a threat of bankruptcy in the next years („safe zone“),
2) Values between 2.7–1.2 – further development cannot be specified more precisely („grey zone“),
3) Values lower than 1.2 – the firm is threatened by the serious financial problems in the next years (“distress zone”).

This paper demonstrates that results of Altman Z-score are influenced by accounting framework. Tests was conducted in company which prepared financial statements for the same year according two different accounting frameworks. Financials statements are available at www.registeruz.sk. Analyzed company decided to change accounting framework to IFRS. Before changing accounting framework this company prepared financial statements according Slovak legislation, but also IFRS.A purpose was also to find the specific items that have caused differences in financial statements.

3. DATA AND RESULTS

Transfer to IFRS is not only formal calculation of numbers, but it means also changing of accounting principles and itis necessary to implement new way of measuring the profitability of company what can influence almost all market transactions and can influence also other financial ratios of company.

Following tables show information from balance sheet and profit and loss statement prepared according Slovak legislation and also according IFRS and there are shown also differences between them.

Table 1. Balance sheet prepared according Slovak legislation and IFRS

	SR	IFRS	Difference
Non-current assets	1581	2507	926
Bank accounts and cash on hand	215	215	0
Receivable	186	186	0
Accruals	541	71	-470
	2523	**2979**	**456**
Equity	200	200	0
Funds created from profit	20	20	0
Not distributed profit	1397	1277	-120
Liabilities related to social fund	57	57	0
Short term liabilities	690	1266	576
Tax liabilities	75	75	0
Deferred tax liability	19	19	0
Provisions	65	65	0
	2523	**2979**	**456**

Source: Financial statements available at www.registeruz.sk

Table 2. Profit and loss statement prepared according Slovak legislation and IFRS

	SR	IFRS	Difference
Consumed raw materials	1471	1471	0
Services	560	430	-130
Wages and salaries	889	889	0
Amortization / depreciation	592	824	232
Financial expenses	3	21	18
Taxes and fees	69	69	0
Profit/loss	367	247	-120
	3951	**3951**	**0**
Revenues from the sale of own products and services	3785	3785	0
Other revenues	165	165	0
Financial income	1	1	0
	3951	**3951**	**0**

Source: Financial statements available at www.registeruz.sk

Differences in financial statements prepared according Slovak legislation and IFRS are caused by costs for products advertising in total amount 200 ths. EUR. According Slovak legislation these costs shall be accrued/deferred (in this case for 4 years), and according IFRS are these costs considered as costs of accounting period in total amount.

Other difference was caused by different reporting of financial lease. Accounting entity rented machinery for 5 years. In financial statements prepared according Slovak legislation this machinery is booked at the lessor´s accounting book. Lessee shall book only accrued/deferred increased payments. Other regular payments are preserved.

Period of leasing	5 years
Lifetime	5 years
Increased payment	400 ths.

Regular payments at the date 31.12. 200 ths.

In the financial leasing contract must be agreed that all substantial risks are transferred to lessee and estimated residual value is 0.
Slovak legislation: accrual/deferral of increased payment 400 / 5 = 80 and regular annual payment 200 ths. EUR.
IFRS: Depreciation from present value of machinery
Present value = 400+200 x (1 / 1,1)+200 x (1 / $1,1^2$)+200 x (1 / $1,1^3$)+200 x (1 / $1,1^4$)+200 x (1 / $1,1^5$)
Present value = 1158,15
Depreciation = 1 158,15 / 5 = 231,63 (rounded 232,–)
Interest costs = 18 ths. EUR

Table 3. Altman Z-score using data from financial statements

	SR	IFRS
net working capital / total assets x 0,717	[(215 + 186 + 541 – 690 -75) / 2523] x **0,717**	[(215 + 186 + 71 – 1 266 -75) / 2979] x **0,717**
retained earnings / total assets x 0,847	[(1397 + 20) / 2523] x **0,847**	[(1277 + 20) / 2979] x **0,847**
EBIT / total assets x 3,107	[(367 + 69 + 3) / 2523] x **3,107**	[(247 + 69 + 21) / 2979] x **3,107**
equity[1] / total liabilities x 0,420	[(200 + 20 + 1397) / (57 + 690 + 75 + 19 + 65)] x **0,42**	[(200 + 20 + 1277) / (57 + 1266 + 75 + 19 + 65)] x **0,42**
sales / total assets x 0,998	(3785 / 2523) x **0,998**	(3785 / 2979) x **0,998**
Total	**3,313**	**2,203**

Source: Own processing

When comparing the results of Altman Z-score we have found out that however we compare financial statements of one company for the same accounting period, the data are significantly different. When we interpret result of Altman Z-score including data from financial statements prepared according IFRS – the company belongs to "grey zone" but when we interpret result of Altman Z-score including data from financial statements prepared according Slovak legislation – the company Z-score is 2,9 and according this result company belongs to "safe zone". It is necessary to mention, that the results of Altman Z-score are also influenced by percentage of differences from total assets.

4. CONCLUSION

Financial analysis and comparison of actual values with historical values can show differences in values and by their correct interpretation we can contribute to better informing of stakeholders. It should help to early detection of possible problems, identification of causes and finding efficient ways of their elimination. Source of data for calculating these models are mainly financial statements or annual report. The aim of this paper is to analyze if changes in accounting rules affect the results of the financial analysis. We have found out that choosing the right model for financial analysis is not satisfactory; the most important is the quality of data used for calculation of models.

Quality of financial statements depends on reliability and economic content of financial statements. Financial statements for accounting period is important source of information for financial analysis. If we use these data correctly, we can analyze history, predict the future and plan activities of company. However financial statement is trustable source of information for financial

[1] Instead of market price of equity we used accounting value of equity from balance sheet.

analysis it has various short comings and limits. There are some pluses and also minuses of using financial statements. The most significant pluses of using financial statements are following:

- It is public source of information,
- It contains data for minimum two accounting periods,
- it is prepared in regular intervals,
- Is prepared with balance sheet continuity principle and it is consistently presented,
- Advantage is also an interconnectedness of financial statements,
- Data from financial statements are comparable.

The most significant minuses of using financial statements are following:

- Changes in accounting legislation,
- Changing of accounting framework,
- Inaccuracies in valuation,
- Failure to take into account an inflation,
- Failure to take into account a deflation,
- Estimations,
- Relativity of data,
- Errors and frauds,
- Window dressing,
- Cumulating of data.

It is obvious that there are more pluses than minuses. This paper illustrated the consequences of changes in accounting framework. This can be eliminated by changing data from financial statements before financial analysis is done and risk of distortion of results can be eliminated. We follow principle of economy – detection of other information, calculation and it makes sense to carry out modifications only if they have important influence on results of financial analysis of company.

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