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Specifics of IFRS Adoption by Czech Private Companies

David Procházka[a,]*

[a]University of Economics, Prague; Department of Financial Accounting and Auditing, W. Churchill Sq. 4, Prague 130 67, Czech Republic

Abstract

The paper assesses the influence of IFRS adoption on management accounting of Czech unlisted companies under foreign control belonging to groups, for which consolidated financial statements in compliance with IFRS are prepared. As these Czech subsidiaries prepare their statutory accounts in compliance with Czech GAAP, IFRS are incorporated into management accounting in order to optimise reporting system costs for meeting information demands of all interested parties. The paper investigates the perception of management on the importance of IFRS for internal decision making. Our results, based on questionnaire survey, show that forced IFRS adopters steadily integrate the IFRS principles into management accounting subsystem. IFRS influence is derived from the structure of executive compensation schemes constructed by parent companies and has impact primarily on the definition of key performance indicators and other financial targets. We find also evidence that with increasing number of areas, in which management accounting utilises the IFRS-based measures, the (subjective) perception of their importance increases, too.

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Keywords: IFRS; Transition country; Unlisted companies; Management accounting; Mandatory, voluntary and forced adoption of IFRS

1. Introduction

The goal of the paper is to assess the influence of IFRS adoption by Czech unlisted companies on their management accounting. We focus on specifics of private companies under foreign control belonging to the groups, for which consolidated financial statements in compliance with IFRS are prepared. As these Czech subsidiaries (had to) prepare their statutory accounts in compliance with Czech GAAP, we expect that IFRS are somehow incorporated into management accounting in order to optimise the structure of their reporting system, meet deadline

* Corresponding author.
E-mail address: prochazd@vse.cz

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and minimise costs for meeting increased information demands. The paper investigates the management's perception of the importance of IFRS for internal decision making. More specifically, we presume that with increasing number of areas, in which management accounting utilises the IFRS-based measures, the (subjective) perception of their importance increases, too. Affirmative evidence on the hypothesis could have two practical implications. Firstly, the growing usage of IFRS in management accounting can witness about a deeper integration of financial and management accounting in private companies and provide additional evidence to international research focusing mainly on listed companies. Secondly, the awareness of IFRS importance in terms of management accounting and groups' information flows may support reporting incentives for producing high-quality financial statements for external users, if IFRS are adopted voluntarily in statutory accounts.

The paper is organised as follows. After the Introduction, the Chapter 2 reviews the relevant literature. With reference to the literature review, the Chapter 3 builds up a model of mutual relationship of financial and management accounting, focusing on specifics of a transition country after the IFRS adoption. The Chapter 4 presents selected empirical results from questionnaire survey. The final chapter concludes.

2. Literature review and hypothesis development

Since the industrial revolution, accounting systems have been broken into two separate modules – financial and management accounting. The distinctive demand for special-purpose information for internal decision-making arose already in the middle of the 19th century; the first peak of the evolution of management accounting was reached in the 1920's (Kaplan 1984). Kaplan (1984)'s and Johnson and Kaplan (1987)'s works were the main impetus for the modern changes in management accounting through introducing innovative techniques, which aim to help managers in their strategically oriented decisions. The progress in information and communication technology has contributed to meeting the increasing and ever-changing information requirements of internal users (Ashton, Hopper, and Scapens 1991), (Hoque, Mia, and Alam 2001), (Mendoza and Bescos 2001). Dual relationship of financial and management accounting (Colwyn Jones and Luther 2005) started to be partially mitigated by an international convergence of internal management accounting techniques (Granlund and Lukka 1998), (Ittner and Larcker 2001). The managers administrate internal business processes respecting the value creation goal (Abdel-Kader and Luther 2006). Managers strive for creating value not only for the owners but for a wide group of stakeholders (customers, employees, etc.) as well. On this interface, management accounting systems for internal users interface with the financial accounting systems for external users. In this context, some authors have started to cope with the terms like "integration of financial and management accounting systems" or "the convergence of financial accounting and the management accounting" (Hemmer and Labro 2008), (Taipaleenmäki and Ikäheimo 2013), (Weißenberger and Angelkort 2011).

The global economy brings new challenges for preparers of financial statements as their users require internationally comparable financial information of high quality. The accounting research addresses mainly the economic consequences of mandatory IFRS adoption by listed companies. Major studies are reviewed by (Brüggemann et al., 2013). There are also a few papers dealing with the consequences of voluntary IFRS adoption by private companies (Francis et al. 2008), (Nobes 2010), (Bassemir 2011), (Matonti and Iuliano 2012), (André, Walton, and Yang 2012), (Yang 2014). Some of the recent studies assess also the impact of IFRS on the management accounting practices (Colwyn Jones and Luther 2005), (Angelkort, Sandt, and Weißenberger 2008), and their integration with financial reporting (Weißenberger and Angelkort 2011) following the changes in key financial indicators (Lantto and Sahlström 2009) and internal performance measures (Wu and Zhang 2009) induced by the mandatory or voluntary IFRS adoption.

We aim at extending these studies by focusing on a specific group of IFRS adopters – so-called forced IFRS adopters. Forced IFRS adopters are those private companies that (a) are forced to adopt IFRS (following the command of a parent company) and simultaneously (b) are not permitted by the regulatory framework of a given jurisdiction to apply IFRS in their individual financial statements on voluntary basis. This combination of entity specific conditions and regulatory framework complements previous studies on a voluntary adoption of IFRS by unlisted companies. However, as IFRS financial statements cannot be published as statutory accounts and the decision on the adoption is made by "outsiders" (not by managers of a subsidiary, but by managers of the parent), the commonly used term "voluntary adoption" does not describe exactly the institutional background. The term