

Two accounting systems

IFRS and Czech GAAP

Similarities and Differences

August 2009



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Preface

International Financial Reporting Standards (**IFRS**) were adopted in 2005 in many countries around the world including, for listed companies, members of the EU. The International Accounting Standards Board (IASB) issued several new, revised and amended standards and International Financial Reporting Interpretations Committee (IFRIC) issued a number of new interpretations. The Ministry of Finance of the Czech Republic amended the Czech accounting system from 1 January 2009 and it is expected that further amendments will come. In general, the ministry primarily seeks to achieve harmonisation of the Czech accounting system with the requirements of the EU accounting directives, but most of the changes at the same time represent movement towards **IFRS**. However, there are still many subtle differences between these two frameworks, which this publication seeks to highlight and explain.

Czech companies that have issued debt or equity securities traded in regulated public markets must use **IFRS** instead of **Czech GAAP** for the preparation of their consolidated and separate (unconsolidated) financial statements. Other enterprises may use **IFRS** instead of **Czech GAAP** for the preparation of consolidated financial statements. The Czech tax base, however, is still based on Czech Generally Accepted Accounting Principles (**Czech GAAP**) regardless of which accounting standards the companies use for the preparation of their financial statements. Consequently, these companies need to understand the similarities and differences between **IFRS** and **Czech GAAP**.

Developments under both frameworks are ongoing, therefore, it is also necessary to take into account changes that occur subsequent to the time when this publication was prepared (June 2009).

This comparative study has been prepared by the group of PricewaterhouseCoopers consultants who work extensively with both financial reporting frameworks.

I believe that this study will be beneficial not only to companies changing over to **IFRS**, but also to the users of financial statements prepared in this manner, and last but not least, to the Ministry of Finance for the purposes of adjusting tax regulations in such a manner that companies using **IFRS** are not burdened in the future with the requirement to report their pre-tax profit under **Czech GAAP**.

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This publication by PricewaterhouseCoopers is for those who wish to gain a broad understanding of the key similarities and differences between two accounting systems: International Financial Reporting Standards (hereinafter referred to as “**IFRS**”) and Czech Generally Accepted Accounting Principles (hereinafter referred to as “**Czech GAAP**”). The first section provides a summary of the similarities and differences between the two systems and then refers to individual detailed parts in the second section, where key divergences between the systems are highlighted and the likely impact of recent harmonisation proposals are explained.

Obviously, no summary publication can do justice to the many differences of the details that exist between **IFRS** and **Czech GAAP**. Although there is already a reasonable degree of affinity between the basic underlying principles of **IFRS** and **Czech GAAP**, important differences in the detailed application remain which could have a material impact on the financial statements. In this publication we have focused especially on the differences most commonly found in practice. When applying the individual accounting frameworks, readers must consult all the relevant accounting regulations, standards and, where applicable, their national law. Listed companies must also follow relevant securities legislation, such as the regulations of the Czech National Bank.

The International Accounting Standards Board (“IASB”) is currently developing a number of projects that will have (often very material) impact on the current standards. One of the projects, which may be key to the further harmonisation of **Czech GAAP** and **IFRS**, is the IASB’s ‘Small and Medium-sized Entities’ project. The outcome from this project may be a good basis for the future direction of the Czech accounting system, which is still set by the Ministry of Finance of the Czech Republic. Further movements in Czech national legislation may be expected in the near future and hopefully those changes will remove some of the topics covered by this publication; however, a key difference in the emphasis on the definition of principles in **IFRS** and predominantly detailed rules (policies) in **Czech GAAP** is likely to remain for some time yet.

This publication refers to **IFRS** accounting standards which were published as at June 2008 and compares them with **Czech GAAP** taking effect on 1 January 2009. Basically, the **Czech GAAP** used in this publication is prescribed for entrepreneurs, any significant differences for banks and other financial institutions, except for insurance companies (hereinafter referred to as “financial institutions”), are explicitly marked in the text.

The structure of this publication is as follows:

	page
Summary of similarities and differences	4-13
Conceptual framework	14-16
Financial statements	17-24
Consolidated financial statements	25-31
Business combinations	32-36
Revenue recognition	37-39
Expense recognition	40-43
Assets	44-58
Liabilities	59-67
Derivatives and hedge accounting	68-70
Other accounting and reporting issues	71-75
Earnings per share	71
Related party transactions	72
Segment reporting	72-73
Discontinued operations	74
Events after the reporting date	74-75
Interim financial reporting	75
Index	76
Glossary	77

Summary of similarities and differences

SUBJECT	IFRS	Czech GAAP	PAGE
General requirements			
Historical cost	Uses historical cost, but intangible assets, property, plant and equipment (PPE) and investment property may be revalued. Derivatives, selected biological assets and most securities must be revalued. Fair value remeasurement is required on the initial measurement of all financial instruments and for business combinations except for formations of JVs and business combinations under common control.	Uses historical cost, except for specific asset components (for instance derivatives and some securities) that are remeasured at fair value. However, initial recognition of all financial instruments is always at cost. Fair value remeasurement is also applied to some so-called "company transformations".	15
Fair presentation override	In rare cases, entities should override the standards where essential to give a fair presentation.	If in rare cases where given accounting policies do not provide a true and fair view, an entity is obliged to proceed in such a manner as to give a true and fair presentation. However the 'true and fair override' cannot trump the explicit requirements stipulated in the Act on Accounting and must be explicitly disclosed.	15
First-time adoption of accounting framework	Full retrospective application of all IFRS effective as at the reporting date for an entity's first IFRS financial statements, with some optional exemptions and limited mandatory exceptions.	It is not directly relevant –since their incorporation, all entities must use an accounting treatment that is in compliance with Czech GAAP . Entities transiting from IFRS to the Czech GAAP (e.g. as a result of delisting) need to develop their own approach – no guidance is available in Czech GAAP .	16
Financial statements			
Reporting currency	Requires the measurement of profit using the functional currency; however, entities may present financial statements in a different currency.	Only the Czech currency.	17
Components of financial statements	Present and comparative balance sheet (newly renamed the 'statement of financial position'), income statement (if prepared separately from the statement of financial position), statement of financial position, statement of changes in shareholders' equity and statement of cash flows, accounting policies and notes. The opening balance sheet of the comparative reporting period needs to be presented when the reporting entity restates the comparative period due to a change in an accounting policy, reclassifications or due to the correction of an error.	Present and comparative balance sheet, income statement, statement of changes in shareholders' equity, cash flow statement and notes including accounting policies and comments. A statement of changes in equity and cash flow statement are not required in a number of cases. Information for two years (current and prior) is disclosed for all statements although it is not explicitly required for the cash flow statement.	18
Balance sheet format	Does not prescribe a particular format; an entity uses a liquidity presentation of assets and liabilities, instead of a current/non-current presentation, only when the liquidity presentation provides more relevant and reliable information. Certain items must be presented on the face of the balance sheet.	A standard format (structure) is prescribed. Only a more detailed analysis or aggregation in specified cases is permitted. The consolidated balance sheet format is more aggregated and less prescriptive.	19
Income statement format	Does not prescribe a standard format, although expenditure must be presented in one of two formats (analysis by function or by nature). Certain items must be presented on the face of the income statement.	A standard format (structure) is prescribed, expenditure must be presented in one of two formats (analysis by function or by nature). Same adjustments as in the case of the balance sheet are permitted. The consolidated income statement format is more aggregated and less prescriptive.	20

SUBJECT	IFRS	Czech GAAP	PAGE
Financial statements (continued)			
Statement of comprehensive income	It is required that all comprehensive income items (i.e. all non-owner changes in net assets) be presented in one statement of comprehensive income or in two primary statements (a separate income statement and a statement of comprehensive income).	Within the changes in shareholders' equity.	20
Exceptional items	Does not use the term, but requires separate disclosure of items that are of such size, incidence (impact) or nature that require separate disclosure to explain the performance of the entity. These items must be presented either on the face of the income statement or in the notes.	Does not use the term. There is a general requirement for the explanation of material items disclosed in the financial statements, although it is not permitted to supplement the prescribed format in the primary structure.	21
Extraordinary items	Prohibited.	Include unusual operations with regard to the normal activities of an entity and cases of random events, changes in accounting methodology and corrections of material prior-period errors. Only entrepreneurs are required to correct prior-period errors through extraordinary items in the current period. Financial institutions correct prior-period errors via restatement of the opening balance of retained earnings of the current period.	21
Statement of changes in shareholders' equity	Changes in equity (net assets) of an entity during a period arising from transactions with owners in their capacity as owners are presented in the statement of changes in equity. Components of comprehensive income are not permitted to be presented in the statement of changes in equity. The statement must be presented as a primary statement.	Comparable to IFRS , however, components of comprehensive income are presented in this statement. Entities other than financial institutions may disclose the movements in equity in the notes instead of a primary financial statement.	21
Statement of cash flows - format and method	Standard headings, but limited flexibility of contents. Use direct or indirect method.	Only basic categories of cash flows and format are determined, using the indirect method (from operating, investing and financial activities). Use of direct or indirect method. Entities may disclose the cash flows statement in the notes instead of a primary financial statement.	22
Statement of cash flows - definition of cash and cash equivalents	Cash includes overdrafts and cash equivalents with short-term maturities (less than 3 months).	Comparable to IFRS , however, certain stamps and vouchers, which do not qualify as financial assets under IFRS are considered cash equivalents (e.g. meal vouchers).	22
Statement of cash flows - exemptions	No exemptions.	Exemption for all entities without the required audit of financial statements. A cash flow statement is not required for all banks and some financial institutions.	22
Changes in accounting policies	Restate comparatives and prior-year opening retained earnings, unless specifically exempted by transitional provisions of a new standard.	Effect of changes is included in extraordinary items of the current period. The first year of accounting for the deferred tax is an exception. The deferred tax is recorded against equity.	23
Correction of material errors	Comparatives are restated and, if the error occurred before the earliest prior period presented, the restated opening balance sheet for the earliest period presented is included in the primary financial statement.	Included in extraordinary items in the income statement of the current period (except for fundamental errors in the case of financial institutions recorded against the retained earnings of prior years).	23
Changes in accounting estimates	Reported in the income statement in the current period and the effect on future periods is disclosed, if applicable.	Comparable to IFRS .	24

Summary of similarities and differences

SUBJECT	IFRS	Czech GAAP	PAGE
Consolidated financial statements			
Definition of subsidiary	Based on voting control or power to govern. Control is presumed to exist when the parent owns, directly or indirectly through subsidiaries, more than one half of an entity's voting power. Control also exists when the parent owns half or less of the voting power but has legal or contractual rights to control, or de facto control (rare circumstances). The existence of currently exercisable potential voting rights is also taken into consideration.	Decisive influence on governance and control of activities through more than a 50% of voting rights or arising from the contract or articles of association of the entity ("governed" or "controlled" company). Currently exercisable voting rights are generally ignored.	25
Special purposes entities ("SPEs")	Consolidate where the substance of the relationship indicates control.	Legal status decisive, subject to consolidation are governed and controlled entities as defined in the Commercial Code. SPEs which are not controlled from the legal point of view, but from which risks and rewards relate mainly to the reporting entity should be disclosed in the notes.	26
Non-consolidation of subsidiaries	Not applicable - all subsidiaries must be consolidated.	If the subsidiary is acquired and held for sale within one year or (rarely) if there are long-term limitations preventing the exercise of control. Stated at cost or using the equity method.	26
Definition of associate	Based on significant influence: presumed if 20% or more voting rights.	Comparable to IFRS .	27
Presentation of associate results	Use equity method. Show share of post-tax result. In standalone financial statements measured at cost or fair value.	Accounted for using method called 'equity accounting'; however, the application of the method is different than in IFRS – no notional purchase price allocation is required. In standalone financial statements, there is an option to account for an associate at cost or using the 'equity method'. In consolidated financial statements, the 'equity method' – based on the carrying amounts in the associate's books - is required.	27
Disclosures about significant associates	Give detailed information on significant associates' assets, liabilities, revenue and results.	Disclosures include names and descriptions of consolidated associates and method of accounting for consolidation.	27
Equity method or proportional consolidation for joint ventures	Both the proportional consolidation and equity method are permitted.	Use of proportional consolidation is mandatorily. Unincorporated joint ventures not addressed in the Czech GAAP – legal status is decisive for accounting.	28
Foreign currency translation – individual companies	Translate transactions at rate on date of transaction; monetary assets/liabilities at balance sheet rate; non-monetary items at historical rate.	No definition of monetary assets/liabilities exists. Resolved by specific examples, interests and shares included. Fixed exchange rates for a specified period can be used. Exchange rates have to be directly derived from the official exchange rates of the Czech National Bank. Other aspects comparable to IFRS .	30
Foreign entities within consolidated financial statements	Use closing rate for balance sheets; average rate for the period for income statements. Take exchange differences to equity. Include in gain or loss on disposal of a subsidiary.	Use closing rate for both balance sheet and income statement. No detailed guidance.	30
Hyperinflation – foreign entity	Adjust local statements of foreign entity to current price levels prior to translation.	No rules. True and fair view must be applied in determining the accounting policy.	31

SUBJECT	IFRS	Czech GAAP	PAGE
Business combinations			
Types	Purchase method has to be used. Business combinations involving entities under common control or formations of joint ventures are not addressed in IFRS .	Business combinations are not treated as a whole. There is different guidance for consolidations, purchase and contribution of a business, and "company transformation". Individual types of transactions are specified in the Commercial Code and are accounted for in accordance with the legal form. No distinction is made between transactions among entities under common control and transactions involving unrelated parties, except for fully owned subsidiary.	32
Purchase method – fair values on acquisition	<p>Purchase consideration, assets, liabilities and contingent liabilities of acquired entity are fair valued. If control is obtained in a partial acquisition of a subsidiary, the full fair value of assets, liabilities and contingent liabilities, including portion attributable to the minority (non-controlling) interest, is recorded on the consolidated balance sheet. Goodwill is either recognised as the 'full goodwill' (including the minority interest portion) or as the residual between the fair value of the consideration paid and the percentage of the fair value of the net identifiable assets acquired.</p> <p>Liabilities for restructuring activities are recognised only when the acquiree has an existing liability as at acquisition date. Liabilities for future losses or other costs expected to be incurred as a result of the business combination cannot be recognised.</p>	<p>Assets and liabilities of the acquired entity are revalued subject to the requirements of the Commercial Code in accordance with the legal form of the transaction (option not to revalue exists in certain circumstances). Only assets and liabilities recognised in the acquirees' balance sheet can be recognised by the acquirer.</p> <p>Banks and other financial institutions: comparable to IFRS. Entrepreneurs: follow some of the basic principles common with IFRS.</p>	32
Purchase method – contingent consideration	Included in cost of combination as at acquisition date if adjustment is probable and can be measured reliably.	No guidance.	32
Purchase method – minority interests at acquisition	State either at the fair value (the 'full goodwill method') or at a share of fair value of net identifiable assets.	State at a share of the acquiree's equity, split into its respective categories	33
Purchase method – goodwill	Either the full goodwill method (the difference between the fair value of the business and the aggregated fair value of the net identifiable assets acquired) or goodwill attributable to the controlling interest (the difference between the fair value of consideration paid and the controlling interest's portion of the fair value of net identifiable assets acquired). Goodwill is not amortised, but it is tested annually for impairment.	Upon acquisition of an entity or its part, capitalise and amortise on a straight line basis over 5 years when an itemised fair value remeasurement of assets was performed, otherwise over 15 years from the acquisition (so-called difference arising upon the acquisition). Different rules, to some extent comparable with IFRS , apply to consolidated financial statements and to financial institutions.	34

Summary of similarities and differences

SUBJECT	IFRS	Czech GAAP	PAGE
Business combinations (continued)			
Purchase method – negative goodwill	Recognised in the income statement immediately.	Upon acquisition of an entity or a part thereof, record negative goodwill as a negative asset (on the asset side of the balance sheet); amortised over 5 years when an itemised fair value remeasurement of assets is used, otherwise over 15 years from the acquisition. In consolidated financial statements, it is recognised as a negative asset and amortised on a straight-line basis in the income statement over a period of up to 20 years. Financial institutions recognise it as a negative asset over the period of use of assets to which it relates. If the respective amortisation period cannot be ascertained reliably, it is amortised over the period of five years as a maximum.	35
Purchase method – subsequent adjustments to fair value	Fair values can be corrected within twelve months window after the acquisition date. Record subsequent adjustments in the income statement.	No detailed rules – once the financial statements are published, no revision of the accounting is allowed. No specific rule regulating creation and reversal of provisions at acquisition.	35
Purchase method – disclosure	Disclosures include names and descriptions of combining entities, date of acquisition, summary of fair values of assets and liabilities acquired, and impact on results and financial position of acquirer.	No specific disclosures are required, except for the name of the combining entities and the date of acquisition.	36
Revenue recognition			
Revenue recognition	Recognise revenue when risks and rewards have been transferred and the revenue can be measured reliably.	No comparable guidance is given on revenue recognition, contractual arrangements drive revenue recognition.	37
Construction contracts	Revenue and profit on long-term contracts accounted for using the percentage of completion method. Completed contract method prohibited.	The percentage of completion method not part of the Czech GAAP . Accounting treatment depends on the form of contractual arrangement, usually having the form of completed contracts, since the inclusion of unrealised profits is not allowed.	38
Expense recognition			
Interest expense	Interest expense recognised on an accrual basis. Effective interest method used to amortise all borrowing costs. Optional relief for assets at fair value through profit and loss.	Contractual interest is recognised on an accrual basis. Other borrowing costs are recognised as incurred. Effective interest rate is only used by financial institutions, with reliefs for short-term (current) assets and fair valued assets.	40
Employee benefits – defined benefit plans	Projected unit credit method is used to determine benefit obligation and record plan assets at fair value. Actuarial gains and losses can be partially deferred (under the corridor method).	Defined benefit plans are not used in practice and are not regulated by any standard.	40

SUBJECT	IFRS	Czech GAAP	PAGE
Expense recognition (continued)			
Employee share compensation	Expense incurred as a result of share compensations are recognised in the income statement. Corresponding amount is recorded either as a liability or an increase in equity depending on whether the transaction is determined to be cash- or equity-settled. Amount to be recognised is measured at the fair value of equity instruments granted.	No guidance is given on recognition or measurement of items. Disclosure of shares used as compensation for members of the Board of Directors, Supervisory Board and executives is required. Cash settled obligations should be recognised as a liability with the corresponding amounts being recorded in the income statement.	42
Employee benefits – termination benefits	Termination benefits arising from redundancies are accounted for similarly to restructuring provisions.	Termination benefits are accounted for similarly to restructuring provisions.	43
Assets			
Acquired intangible assets	Capitalise if recognition criteria are met; intangible assets may have indefinite useful life or are amortised over useful life. Intangible assets with indefinite useful life are tested for impairment annually. Revaluations are permitted in rare circumstances.	Capitalise if definition of intangible assets is met; amortise over their useful life. Revaluations and indefinite life are not permitted.	44
Internally generated intangible assets	Expense research costs as they are incurred. Capitalise and amortise development costs only if stringent recognition criteria are met.	Research and development costs are capitalised if the assets are held for sale. Other costs of internally-generated intangible assets held for repetitive sale are also capitalised. Internally incurred costs for development software for own use are expensed.	45
Property, plant and equipment	Use historical costs or revalued amounts. Frequent revaluations of entire classes of assets are required when the revaluation option is chosen. Component approach must be applied in determining depreciation for property, plant and equipment.	Use of historical cost (also replacement cost in rare cases). Revaluation is permitted only upon acquisition of an entity or certain company transformations. Spare parts are inventory and not property, plant and equipment. Component approach is not allowed under CZ GAAP until 1 Jan 2010.	46
Non-current assets held for sale or disposal group	Non-current assets are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. A non-current asset classified as held-for-sale is measured at the lower of its carrying amount and fair value less costs to sell. Comparative balance sheet is not restated.	No guidance – assets are presented and measured under other asset categories on the balance sheet until derecognition.	48
Leases – classification	Leases are classified as finance leases if substantially all risks and rewards of ownership transferred to a lessee. Substance rather than legal form is important.	Legal form prevails over the commercial substance. Consequently, there is no difference in accounting for finance and operating leases.	49
Leases – lessor accounting	Record amounts due under finance leases as a receivable (financial asset). Allocate gross earnings to give constant rate of return based on (pre-tax) net investment method.	The leased assets (both finance and operating) are capitalised and depreciated by the lessor for both finance and operating leases. Revenue is accrued over the lease term on a straight line basis.	49
Impairment of non-financial assets	If impairment indicated, write down assets to higher of the fair value less cost to sell and the value in use based on discounted cash flows. If no impairment loss arises, reconsider useful lives of those assets. Reversals of losses permitted in certain circumstances, except for goodwill.	Only general requirement to reflect possible impairment. No detailed guidance given for the measurement, in practice the basic principles from IFRS are used. Permanent impairment (recognised by a one-off write-down) or temporary impairment (provisions are created that may be reversed) are distinguished.	50

Summary of similarities and differences

SUBJECT	IFRS	Czech GAAP	PAGE
Assets (continued)			
Capitalisation of borrowing costs	Permitted, but not required, for qualifying assets (inventory may be a qualifying asset). Effective from 1 January 2009 borrowing costs must be capitalised.	Capitalised contractual interest, not full borrowing costs. Capitalisation limited to borrowings specifically received to obtain an item of fixed asset. Interest on loans for the acquisition of purchased inventory is not capitalised.	51
Investment property	Measure at depreciated cost less accumulated amortisation or fair value and recognise changes in fair value in the income statement.	No specific guidance; investment property treated as property, plant and equipment.	51
Inventories	Carried at lower of cost and net realisable value. Use FIFO or weighted average method to determine cost. LIFO prohibited. Reversal is required for subsequent increase in value of previous write-downs. Borrowings costs related to inventories, which are qualifying assets, are capitalised.	Comparable to IFRS , however borrowing costs related to purchased inventories are never capitalised.	52
Biological assets	Measured at fair value less estimated point-of-sale costs (marketing costs).	No specific guidance. Treated as inventories or fixed assets, fair value measurement not permitted.	53
Financial assets – measurement	Depends on financial asset's category – if held to maturity or loans and receivables, then carried at amortised cost, otherwise at fair value. Unrealised holding gains/losses on assets at fair value through profit or loss are recognised in the income statement, and on available-for-sale investments recognised in equity.	Comparable to IFRS . Insurance companies record available-for-sale securities in the income statement, held-to-maturity securities are fair valued through equity. The definitions of categories slightly differ, full fair value option is allowed for securities designated at fair value through profit and loss. Shares in other than joint stock companies are measured at cost less impairment.	54
Derecognition of financial assets	Derecognise financial assets based on risks and rewards first; control is secondary test.	Accounting treatment follows legal form. Financial institutions derecognise financial assets based on control test.	57
Liabilities			
Provisions – general	Record the provisions related to present obligations from past events if outflow of resources is probable and can be reliably estimated. Where the effect of the time value of money is material, the amount of a provision shall be the present value of the obligation.	Provisions created for possible risks and expected losses. Furthermore, provisions for future repairs of property, plant and equipment are created (not permitted under IFRS). Financial institutions comparable to IFRS . No discounting is required for measurement – however entities may factor in the time value of money.	59
Provisions – restructuring	Recognise restructuring provisions if detailed formal plan announced or implementation effectively begun.	Based on the approved restructuring plan a provision for this restructuring may be created, no announcement needed.	59
Contingencies	Disclose unrecognised possible losses and probable gains.	Certain contingencies may be recognised as liabilities (no strict recognition and measurement guidance provided).	61
Deferred income taxes – general approach	Use full provision (liability) method driven by balance sheet temporary differences. Deferred tax assets are recognised if recovery is probable (more likely than not).	Comparable to IFRS .	62

SUBJECT	IFRS	Czech GAAP	PAGE
Liabilities (continued)			
Deferred income taxes – main exceptions	Non-deductible goodwill and temporary differences on initial recognition of assets and liabilities that do not impact on accounting or taxable profit.	Entrepreneurs shall recognise deferred tax on all temporary differences – no initial recognition exemption applies. Financial institutions similarly to IFRS do not take into account non-deductible goodwill.	62
Government grants	Recognised as deferred income and amortised when there is reasonable assurance that the entity will comply with the conditions attached to them and the grants will be received. Entities may offset capital grants against asset values.	Comparable to IFRS . Capital grants must always be offset against asset values.	64
Leases – lessee accounting	Record finance leases as asset and obligation for future rentals. Normally depreciate over useful life of asset. Apportion rental payments to give constant interest rate on outstanding obligation. Operating lease rentals are charged on straight-line basis.	Accounting for finance and operating leases is the same; generally charge rentals on a straight-line basis.	64
Leases – sale and leaseback transactions	For a finance lease, defer and amortise profit arising on sale and finance leaseback. If an operating lease arises then profit recognition depends on sale proceeds compared to fair value of the asset. Substance/linkage of transactions is considered.	Sale and leaseback not addressed specifically, but legal form of transaction takes precedence over commercial substance, i.e. both transactions are recorded separately.	65
Financial liabilities – classification	Classify capital instruments depending on substance of the issuer's obligations, as either liability or equity. Mandatorily redeemable preference shares are generally classified as liabilities, rather than equity.	Accounting treatment follows the legal form. Instruments that are neither shares nor equity interests classify as liabilities. Fixed interest payable on preference shares is prohibited by law.	66
Convertible debt	Account for convertible debt on split basis, allocating proceeds between equity and debt.	Conventional convertible debt is usually recognised entirely as liability, in practice rarely used financial instrument. Financial institutions need to separate the embedded derivative.	66
Derecognition of financial liabilities	Derecognise liabilities when extinguished. The difference between the carrying amount and the amount paid is recognised in the income statement.	Accounting treatment follows the legal form. Financial institutions comparable to IFRS .	67
Equity instruments			
Capital instruments – purchase of own shares	The full amount paid show as deduction from equity.	Comparable to IFRS .	67

Summary of similarities and differences

SUBJECT	IFRS	Czech GAAP	PAGE
Derivatives and hedge accounting			
Derivatives and other financial instruments – measurement of financial instruments and hedging activities	<p>Measure derivatives and hedge instruments at fair value; recognise changes in fair value in income statement except for effective cash flow hedges, where the changes are deferred in equity until effect of the underlying transaction is recognised in the income statement.</p> <p>Gains/losses from hedge instruments that are used to hedge future non-financial assets are included in cost of an asset/liability, for financial assets are retained in equity and released in the income statement, together with effects of the hedged item.</p>	Comparable to IFRS .	68
Embedded derivatives	Embedded derivatives separated from the host contract unless the whole instrument is measured at fair value or the economic characteristics and risks of the embedded derivative are the same as those of the host contract.	Entrepreneurs can elect not to separate embedded derivatives. Other provisions are comparable to IFRS . Financial institutions follow guidance close to IFRS . Non-financial contracts in foreign currency are generally considered to be closely related to the host contract.	68
Derivatives and other financial instruments – measurement of hedges of net investments in foreign operations	<p>Gains/losses on hedges of net investments in foreign operations are recognised in equity, including hedge ineffectiveness on non-derivatives. For derivatives, record hedge ineffectiveness in the income statement.</p> <p>Gains/losses held in equity must be transferred to the income statement on disposal of investment.</p>	Comparable to IFRS , however the concept of net investment of a foreign operation is not further developed in Czech GAAP .	68
Other accounting and reporting issues			
Earnings per share – diluted	Use weighted average potential dilutive shares as denominator for diluted EPS. Use “treasury stock” method for share options/warrants.	No standard (guidance) or disclosure requirements for EPS (except for investment funds and mutual funds, which recognise only the basic earnings per share in the notes).	71
Disclosure of risks arising from financial instruments	Entity shall disclose information enabling users of financial statements to evaluate the nature and extent of risks arising from financial instruments to which the entity is exposed.	If relevant for financial position or result, entity using financial instruments must disclose in its annual report its goals and methods of risk management and information on price, credit and liquidity risk exposures.	71
Related party transactions – definition	Determine by level of direct or indirect control, joint control and significant influence of one party over another or common control of both parties.	The definition of related party refers directly to IFRS as adopted by the EU.	72

SUBJECT	IFRS	Czech GAAP	PAGE
Other accounting and reporting issues (continued)			
Related party transactions – disclosures	Name of the parent entity is disclosed and, if different, the ultimate controlling party, regardless of whether transactions with those parties occur. For related party transactions, nature of relationship (seven categories), amount of transactions, outstanding balances, terms and types of transactions are disclosed. Disclosure of compensation of key management personnel on an aggregate basis is required within the financial statements.	Disclosure of material transactions with related parties, which were not conducted on an arm's length basis. Disclosure of compensation of key management personnel is required aggregated by the board, supervisory board and total for executive officers.	72
Segment reporting – scope and basis of formats	Applies to public entities and entities that file, or are in the process of filing, financial statements with a regulator for the purposes of issuing any instrument in a public market. Reporting of operating segments is based on those segments reported internally to entity's chief operating decision-maker for purposes of allocating resources and assessing performance.	No specific guidance. All entities must report split of revenue from ordinary activities by main activities divided also between domestic and export sales.	72
Discontinued operations – definition	Operations and cash flows that can be clearly distinguished for financial reporting and represent a separate major line of business or geographical area of operations, or a subsidiary acquired exclusively with a view to resale.	No guidance.	74
Discontinued operations – presentation and main disclosures	At a minimum, a single amount is disclosed on face of income statement, and further analysis disclosed in notes, for current and prior periods. Assets and liabilities of discontinued operations are presented separately from other assets and liabilities on balance sheet. No restatement of comparative balance sheet.	No guidance. However, if the impact on the financial position of the entity is material, relevant disclosures should be provided in the notes.	74
Events after the reporting date	Adjust financial statements for subsequent events, providing evidence of conditions at balance sheet date and materially affecting amounts in financial statements (adjusting events). Disclose non-adjusting events.	Principles comparable to IFRS , but no specific and detailed guidance available.	74
Interim financial reporting	Content is prescribed and basis should be consistent with full-year statements. Frequency of reporting (eg. quarterly, semiannually) is imposed by local regulator or at discretion of entity.	No requirement for interim reporting under Czech GAAP . Public companies prepare interim reports under IFRS .	75

CONCEPTUAL FRAMEWORK

IFRS includes a conceptual framework. The principles set out in this framework provide a basis for setting accounting standards, and a point of reference for the preparation of financial information where no specific guidance exists. The Czech Republic is a member of the European Union and therefore the EU accounting directives (4th EU Directive on annual company financial statements and 7th EU directive on consolidated financial statements) represent an underlying regulation, which is implemented into the national law. **Czech GAAP's** basis is articulated in the Act on Accounting. This Act stipulates basic accounting principles and requirements for bookkeeping; however, there is no conceptual framework prepared on a coherent basis, including definitions of basic terms. Detailed accounting rules comprising accounting methods applicable to certain types of transactions are included in accounting decrees of the Ministry of Finance (one decree sets rules for entrepreneurs and one decree for financial institutions) and in Czech Accounting Standards (CUS) also issued by the Ministry of Finance. The National Accounting Board, an umbrella organisation covering the Chamber of Auditors, Chamber of Tax Advisors, Union of Accountants and the Finance and Accounting Faculty of the Prague University of Economics, are issuing legally non-binding interpretations of unclear issues which are in practice gradually accepted as best practise.

Qualitative characteristics of financial information

IFRS Financial information must possess certain characteristics for it to be useful. The **IFRS** framework requires that financial information be understandable, relevant, reliable and comparable.

Czech GAAP Information disclosed in the financial statements must be understandable, reliable, comparable and is considered from the viewpoint of materiality (comparable to **IFRS**). A general rule applies that entities are obliged to maintain their account books in a manner that is correct, complete, conclusive, understandable, clearly arranged and ensuring permanence of the accounting records. In exceptional cases, where reporting in accordance with accounting decrees and/or CUS would not provide true and fair presentation of transactions or events, reporting entities are required to adopt accounting policy departing from the prescribed rules in order to achieve true and fair presentation and disclose the circumstances. However, the accounting policies adopted by reporting entities shall never depart from the rules prescribed in the Act on Accounting. The substance over form principle, applicable within **IFRS**, is replaced in **Czech GAAP** by the requirement for selection of a method providing true and fair presentation of substance within legal form, however, not beyond it (see accounting for finance leases).

Reporting elements

IFRS The **IFRS** framework presents five reporting elements: assets, liabilities, equity, income (includes revenues and gains) and expenses (includes losses).

Assets are resources controlled from a past event. Liabilities are present obligations arising from a past event. Assets and liabilities are recognised in the statement of financial position when it is "probable" that economic benefits will flow in to or out from the entity, and those benefits must be able to be measured reliably.

Equity is the residual interest in the assets after deducting the entity's liabilities.

Income is increases in economic benefits that result in increases in equity other than those relating to contributions from equity participants. Expenses are decreases in economic benefits that result in decreases in equity other than those relating to distributions to equity participants.

CONCEPTUAL FRAMEWORK (continued)**Reporting elements (continued)**

Czech GAAP The Czech accounting legislation refers to the same components of accounting recognition (i.e. property, including assets; payables, including liabilities; equity; income and expenses) – however, definitions of these basic terms are not available. Certain items of these basic components have been defined in Czech accounting standards, especially for financial institutions, however, the key definitions are interpreted using past practice and academic literature.

HISTORICAL COST

IFRS Historical cost is the main accounting convention. However, **IFRS** permits the revaluation of intangible assets, property, plant and equipment (PPE) and investment property. **IFRS** also requires measurement at fair value of certain categories of financial instruments and certain biological assets.

Czech GAAP Historical cost convention is applied to most asset and liability components. Only certain securities (except for held-to-maturity securities, non-tradeable bonds, securities representing an ownership interest with dominant or significant influence and securities issued by an entity), derivatives, financial placements and technical reserves of insurance companies, assets and liabilities in some transformations of companies or cooperatives and the portion of assets and liabilities hedged with derivatives under fair value hedges, are measured at fair value. Fair value is also a measurement basis for receivables held for trading and all trading liabilities similarly to **IFRS**. Equity shares in other than joint stock companies are measured at cost less impairment.

FAIR PRESENTATION OVERRIDE AND PRIORITY OF SUBSTANCE OVER LEGAL FORM

IFRS For assessment and presentation of information, the commercial substance is taken into account, not just its legal form. Entities may depart from a standard in extremely rare circumstances, in which compliance with a requirement in **IFRS** would result in presentation of misleading financial information. **IFRS** requires disclosure of the nature of and the reason for the departure and the financial impact of the departure. The override does not apply where there is a conflict between local company law and **IFRS**; in such a situation, the **IFRS** requirements must be applied.

Czech GAAP If in very rare cases the application of accounting methods is inconsistent with “fair presentation”, an entity shall proceed in such a manner to ensure adherence to the fair presentation. This fact, including the justification and disclosure of the impact on assets, liabilities, financial position and profit/loss, is disclosed in the notes to financial statements. However, the accounting treatment adopted by reporting entities shall never depart from the rules prescribed in the Act on Accounting.

FIRST-TIME ADOPTION OF ACCOUNTING FRAMEWORK

- IFRS** The **IFRS** framework includes a specific standard on how to apply **IFRS** for the first time. It introduces certain reliefs and imposes certain requirements and disclosures. First-time adoption of **IFRS** as the primary accounting basis requires full retrospective application of **IFRS** effective as at the reporting date for an entity's first **IFRS** financial statements, with exemptions, for example for property, plant and equipment and other assets, business combinations and pension plan accounting. Comparative information must be prepared and presented on the basis of **IFRS**. Almost all adjustments arising from the first-time application of **IFRS** must be made against opening retained earnings of the first period presented on the **IFRS** basis. Some adjustments are made against goodwill or against other classes of equity.
- Czech GAAP** This issue is not directly addressed – all Czech reporting entities must, since their incorporation, maintain their account books in compliance with the Act on Accounting and other relevant regulation. When the Act on Accounting and/or accounting regulations are updated, the transition to the new regulations is ruled by the respective transitional provisions. Entrepreneurs normally recognise the impact in the extraordinary income or expense, financial institutions in equity. There is no guidance given on the transition to **Czech GAAP** from **IFRS**, which may be relevant to some entities after de-listing or on redemption of public debt. Czech companies have to maintain records for income tax purposes, which are based on **Czech GAAP**, even when they use **IFRS** for their statutory financial reporting.

REFERENCES: IFRS: Conceptual framework , IAS 1, IAS 16, IAS 38, IAS 39, IAS 40, IAS 41, **IFRS 1**. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll., Czech accounting standards.

FINANCIAL STATEMENTS

GENERAL REQUIREMENTS

Compliance

IFRS Entities must disclose that financial statements comply with **IFRS**. Financial statements must not disclose compliance with **IFRS** unless they comply with all the requirements of each applicable standard and each applicable interpretation.

Czech GAAP Entities that are issuers of securities registered in regulated securities markets in EU Member States use **IFRS** in their accounting and preparation of their company financial statements and consolidated financial statements. Other entities must account and prepare their company financial statements in compliance with the Act on Accounting and related regulation; for consolidated financial statements **IFRS** may be used instead of **Czech GAAP**.

Reporting currency for presentation of financial statements

IFRS **IFRS** specifies the functional currency as the currency of the primary economic environment in which the entity operates or a currency that has a material impact on the entity.

An entity may choose to present its financial statements in a different currency from the functional currency. The method of translating from the functional currency to the presentation currency is that all balance sheet items except for retained earnings are translated at closing rate. Retained earnings and all profit or loss items are translated at actual rates on transactions dates or at average rates for practical purposes - all the resulting exchange differences shall be recognised as a separate component of equity.

Czech GAAP Account books of are maintained in monetary units of the Czech currency; in certain cases they are also maintained in a foreign currency. Financial statements must be prepared in the Czech currency. For translations of consolidated investments, normally the reporting date exchange rates are used (also for the income statement); however, there are no specific rules for such translations.

Reporting in a hyperinflationary economy

IFRS Where the reporting entity itself reports in the currency of a hyperinflationary economy, it must prepare financial statements based on the measuring unit current as at the reporting date. Comparative amounts for prior periods are also restated in the measuring unit as at the current reporting date. Any gain or loss on the net monetary position arising from the restatement of amounts in the measuring unit current as at the reporting date must be included in net income and separately disclosed.

Czech GAAP No guidance exists (there has never been a hyperinflationary economy in the Czech Republic).

GENERAL REQUIREMENTS (continued)**Components of financial statements**

A set of financial statements under **IFRS** and **Czech GAAP** comprises the following components.

COMPONENT	PAGE	IFRS	Czech GAAP
Statement of financial position/ Balance sheet	18	✓	✓
Income statement	19	(a)	✓
Statement of comprehensive income	19	✓(a)	Not applicable
Statement of changes in equity	20	✓(c)	✓ (c), (d)
Statement of cash flows	21	✓	✓(b), (d)
Notes comprising a summary of significant accounting policies and other explanatory information	-	✓	✓

✓ Mandatory

- (a) Under **IFRS**, an entity shall present all items of income and expense recognised in a period in a single statement of comprehensive income, or in two statements: a statement displaying components of profit or loss (separate income statement) and a second statement beginning with profit or loss and displaying components of other comprehensive income (statement of comprehensive income).
- (b) Financial institutions do not prepare it mandatorily and in practice it is not prepared under **Czech GAAP**.
- (c) Under **IFRS**, the statement includes total comprehensive income for the period and amounts of transactions with owners. Under **Czech GAAP** the statement includes gains and losses not recognised in the income statement.
- (d) Not mandatory, however, most companies prepare those statements in order to achieve true and fair presentation.

Comparatives

IFRS Requires one year of comparatives for all numerical information in the financial statements, with small exceptions. A statement of financial position as at the beginning of the earliest comparative period presented needs to be disclosed, when an entity applies a new accounting policy retrospectively or makes a retrospective restatement of items in its financial statements.

Czech GAAP Requires one year of comparatives for all numerical information in the financial statements and the annual report, with small exceptions.

STATEMENT OF FINANCIAL POSITION/BALANCE SHEET

Both accounting systems require the submission of the statement of financial position as the primary financial statement.

Format

IFRS Does not prescribe a particular statement format, except that **IFRS** requires separate presentation of total assets and total liabilities. Management may use judgement regarding the form of presentation in many areas. Entities present current and non-current assets, and current and non-current liabilities, as separate classifications on the face of the statement except when a liquidity presentation provides more relevant and reliable information. In such cases, all assets and liabilities shall be presented broadly in order of liquidity. However, as a minimum, **IFRS** requires presentation of the following items on the face of the statement:

Assets: property, plant and equipment (PPE), investment property, intangible assets, financial assets, investments accounted for using the equity method, biological assets, inventories, trade and other receivables, current and deferred income tax assets, cash and cash equivalents and assets qualified as held for sale; and

Equity and liabilities: issued share capital and other components of shareholders' equity, minority interest presented within equity, financial liabilities, provisions, trade and other payables, current and deferred income tax liabilities, payables and liabilities included in disposal groups.

Czech GAAP Mandatory minimum scope, structure and classification of balance sheet items are prescribed in accordance with the 4th EU Directive. These items may be specified in more detail or aggregated. Zero items, similarly as in **IFRS**, are not presented. Financial institutions have a specific format in compliance with the relevant EU Directive.

Current/non-current distinction

IFRS The current/non-current distinction is obligatory (except when a liquidity presentation is used). Where the distinction is made, assets must be classified as current assets where they are held for sale or consumption in the course of its normal operating cycle, provided the normal operating cycle is clearly identifiable. Both assets and liabilities are classified as current where they are held for trading, or expected to be realised within 12 months of the reporting date (when the normal operating cycle criterion is not applicable). Interest-bearing liabilities are classified as current when they are due to be settled within 12 months of the reporting date, even if the original term was for a period of more than 12 months; and an agreement to refinance, or to reschedule payments, on a long-term basis is completed after the reporting date and before the financial statements are authorised for issue.

Czech GAAP The current/non-current distinction, except for accruals/deferrals, is mandatory. For tangible and intangible assets, their expected useful life (more than one year) and cost exceeding a certain level determined by a reporting entity are decisive (taking into account true and fair presentation). Non-current financial assets include securities held without intention to use them for trading. For receivables and payables (including loans), residual maturity as at the reporting date (within one year or more than one year) is decisive. No current/non-current distinction is made on the face of the statement of financial position of financial institutions, which disclose mandatorily the residual maturity analysis in the notes to financial statements.

STATEMENT OF FINANCIAL POSITION/BALANCE SHEET (continued)**Offsetting assets and liabilities**

IFRS Assets and liabilities must not be offset, except where specifically permitted by a standard. Financial assets and financial liabilities may be offset where an entity has a legally enforceable right to set off the recognised amounts and intends to settle transactions on a net basis or to realise the asset and settle the liability simultaneously. A master netting agreement, in the absence of the intention to settle net or realise the asset and liability simultaneously, is not sufficient to permit net presentation of derivative financial instruments. Master netting arrangements generally do not meet the conditions of offsetting.

Czech GAAP Offsetting assets and liabilities, expense and income is not permitted, except for:

- a) credit notes or refunds relating to a particular expense or income item and pertaining to an accounting period in which such expense or income was incurred;
- b) income tax re-assessments and refunds, indirect taxes and fees, including offsetting of deferred tax asset and deferred tax liability for one legal entity;
- c) differences ascertained during stocktaking that have arisen in the same stocktaking period probably by unintentional substitutions of inventory types;
- d) provisions (general and specific), and deferred comprehensive expenses; and
- e) foreign exchange differences (gains/losses), gains and losses on revaluation of assets and liabilities,
- f) offsetting of receivables from and payables to the same party denominated in the same currency and with maturities within one year.

INCOME STATEMENT/STATEMENT OF COMPREHENSIVE INCOME

Both accounting frameworks require prominent presentation of an income statement/statement of comprehensive income as a primary statement(s) (although under **IFRS** it is possible to present comprehensive income in two separate primary statements, in this section of the publication we refer just to the statement of comprehensive income when discussing requirements for both the statements).

Format

IFRS **IFRS** does not prescribe a standard format for the statement of comprehensive income. The entity must analyse its expenses by function or by nature. The portion of profit or loss and comprehensive income attributable to the minority interest and to the owners of the parent is separately disclosed on the face of the statement of comprehensive income. Disclosure of expenses by nature is required in the footnotes if functional presentation is used on the statement of comprehensive income.

As a minimum, **IFRS** requires presentation of the following items on the face of the statement of comprehensive income: revenue; finance costs; share of after-tax results of associates and joint ventures accounted for using the equity method; tax expense; post-tax profit or loss of discontinued operations and post-tax gain or loss from disposal of assets constituting the discontinuing operations; net profit or loss; each component of other comprehensive income classified by nature; share of the other comprehensive income of associates and joint ventures accounted for using the equity method; and total comprehensive income.

An entity that discloses an operating result should include all items of an operating nature, including those that occur irregularly or infrequently or are unusual in amount.

INCOME STATEMENT/STATEMENT OF COMPREHENSIVE INCOME (continued)**Format (continued)**

Czech GAAP Mandatory minimum scope, structure and classification of income statement items are prescribed. These items may be specified in more detail or aggregated. Zero items, similar to **IFRS**, are not disclosed. Expenses may be presented in one of two formats (by function or by nature). When the by function presentation format is used, certain items classified by nature have to be disclosed in the notes, similar to **IFRS**. No statement of comprehensive income is used.

Exceptional items

IFRS **IFRS** does not use the term “exceptional items” but requires the separate disclosure of items of comprehensive income that are of such size, nature or impact that their separate disclosure is necessary to explain the performance of the entity for the period. Disclosure may be on the face of the statement of comprehensive income or in the notes.

Czech GAAP Comparable to **IFRS**, **Czech GAAP** does not use this term and in practice exceptional items are either included within extraordinary items (see below) or disclosed in the notes only.

Extraordinary items

IFRS Prohibited.

Czech GAAP The concept of extraordinary expenses and income is broadly defined. These items are defined as transactions of an unusual nature, i.e. activities other than the ordinary activities of the entity, as well as “extraordinary events” which occur incidentally, for instance: change of accounting method, restructuring provisions and provisions for other extraordinary expenses (costs), material adjustments (corrections) to previous reporting periods, income and expenses on assignment or discontinuance of business activity and claims for insurance compensation for extraordinary damage. Also, a vendor records disposal of business in extraordinary income or expense. Extraordinary items are disclosed on the face of the income statement after profit on ordinary activities after tax, but before minority interests in consolidated financial statements. Disclosure of the tax impact of extraordinary items is also provided on the face of the income statement. Any changes in accounting method must also be explained in the notes together with the reason for the change and an assessment of the financial effect on the financial statements.

The scope of extraordinary items for financial institutions is considerably limited (no errors are allowed to be presented as extraordinary items) and is close to the approach applied under **IFRS**.

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

IFRS The statement must be presented as a primary statement. The statement shows total comprehensive income for the period and capital transactions with owners for each component of equity.

Czech GAAP Companies usually prepare the statement as a primary statement although, except for financial institutions, it is possible to present changes in equity within the notes to financial statements.

STATEMENT OF CASH FLOWS**Exemptions**

IFRS No exemptions.

Czech GAAP Financial institutions do not prepare the statement. Other companies prepare the statement although it is not explicitly required.

Direct/indirect method

IFRS Requires that the statement of cash flows reports inflows and outflows of “cash and cash equivalents”. The statement of cash flows may be prepared using either the direct method (cash flows derived from aggregating cash receipts and payments associated with operating activities) or the indirect method (cash flows derived from adjusting net income for transactions of a non-cash nature such as depreciation). The latter is more common in practice.

Czech GAAP Comparable to **IFRS**. Both methods, direct and indirect, are permitted. The latter is almost exclusively used in practice.

Definition of cash and cash equivalents

IFRS Cash may include overdrafts repayable on demand but does not include short-term bank borrowings, changes in which are considered to be financing cash flows. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and that are subject to an insignificant risk of changes in value. A non-equity investment normally qualifies as a cash equivalent only when it has a maturity of three months or less from its acquisition date.

Czech GAAP The definition of cash and cash equivalents is, in practice, comparable to **IFRS**; however certain stamps and vouchers, which do not qualify as financial assets under **IFRS**, are considered to be cash equivalents (e.g. meal vouchers).

Format

IFRS Requires separate classification of cash flows from operating, investing and financing activities.

Czech GAAP Comparable to **IFRS**. Requires separate classification of cash flows relating to transactions that constitute extraordinary profit/loss, cash flows related to the collection and disbursement of dividends or share in profit, and payment of the income tax.

STATEMENT OF CASH FLOWS (continued)**Classification of specific items**

IFRS and **Czech GAAP** require the classification of interest, dividends and tax within specific categories of the cash flow statement. These are set out below:

ITEM	IFRS	Czech GAAP
Interest paid	Operating or financing	Operating, financing (investing (a))
Interest received	Operating or investing	Comparable to IFRS
Dividends paid	Operating or financing	Financing
Dividends received	Operating or investing	Comparable to IFRS
Taxes paid	Operating – unless specific identification with financing or investing	Comparable to IFRS

(a) Paid capitalised interest is shown as a separate item of cash flows from investing activities or as a disclosure in the notes.

CHANGES IN ACCOUNTING POLICIES AND OTHER ACCOUNTING CHANGES**Changes in accounting policies**

IFRS Voluntary changes in accounting policies are allowed only if the change results in reliable and more relevant financial information. Changes in accounting policies should be accounted for retrospectively with comparative information restated and the amount of the adjustment relating to prior periods adjusted against the opening balance of retained earnings of the earliest period presented. An exemption applies when changing comparative information is impracticable.

Policy changes made on the adoption of a new standard must be accounted for in accordance with that standard's transitional provisions. If transitional provisions are not specified then the method described above must be used.

Czech GAAP Similar to **IFRS**, voluntary changes in accounting policies are allowed only if the change results in more relevant financial information. Changes in accounting policies must be shown as extraordinary items of the current period. Material changes in measurement methods, depreciation procedures and accounting policies should be disclosed and justified. Changes in accounting policies for the deferred tax are recorded against prior years' retained earnings/accumulated losses.

Corrections of errors

IFRS Requires the same method as for policy changes. An entity must restate comparatives.

Czech GAAP Prior period material errors are recorded as extraordinary items of the current period; comparative amounts are not restated, but restatement (rather than remeasurement) of corresponding amounts is required (if applicable). Financial institutions record corrections of fundamental errors against prior years' retained earnings/accumulated losses. Other (non-fundamental) corrections are recorded within operating result. The financial institutions approach is being discussed for general implementation.

CHANGES IN ACCOUNTING POLICIES AND OTHER ACCOUNTING CHANGES (continued)

Changes in accounting estimates

IFRS Changes in accounting estimates are accounted for prospectively in the statement of comprehensive income when identified. **IFRS** treats changes in depreciation method and revised asset useful lives as a change in accounting estimate.

Czech GAAP Comparable to **IFRS**. No explicit guidance is given on changes in depreciation method or asset useful lives.

REFERENCES: IFRS: IAS 1, IAS 7, IAS 8, IAS 21, IAS 29, SIC-18, SIC-19. **Czech GAAP:** Act on Accounting, Decree 500 and 501/2002 Coll., Czech accounting standards.

CONSOLIDATED FINANCIAL STATEMENTS

PREPARATION

- IFRS** Requires the preparation of consolidated financial statements by a parent entity that includes all subsidiaries. An exemption applies exclusively to a parent that is wholly owned by another entity or provided that it obtains consent of minority owners and its securities are not publicly traded; it is not in the process of issuing securities in public securities markets; and the immediate or ultimate parent publishes consolidated financial statements that comply with **IFRS**.
- Czech GAAP** A company has an obligation to prepare consolidated financial statements when it has subsidiaries. An exemption from the consolidation obligation exists, when at the reporting date at least two of the three limits listed below are not exceeded:
- aggregate amount of gross assets deemed to be consolidated must not exceed CZK 350 million (net of accumulated depreciation, valuation allowances and other corrections)
 - aggregate turnover must not exceed CZK 700 million
 - average adjusted aggregate number of employees for the period must not exceed 250 people.
- This exemption does not apply to entities that are issuers of securities traded on public market and to banks and insurance companies that follow different criteria. Further, exempt from the obligation to prepare consolidated financial statements is a parent that is at the same time a subsidiary consolidated by another parent based in the EU, provided it does not issue publicly traded securities.

SUBSIDIARIES

Definition

The definition of a subsidiary, for the purpose of consolidation, is an important distinction between the two frameworks.

- IFRS** Focuses on the concept of control in determining whether a parent/subsidiary relationship exists. Control is the parent's power to govern the financial and operating policies of a subsidiary to obtain benefits. Control is presumed to exist when a parent owns, directly or indirectly through subsidiaries, more than one half of an entity's voting power, unless it can be clearly demonstrated that such ownership does not constitute control. Control also exists when a parent owns half or less of the voting power but has legal or contractual rights to control the majority of the entity's voting power or votes in the entity's board of directors. In rare situations, control exists through an entity (the parent) holding and voting a large block of shares (but less than 50%) in the other entity in circumstances where the majority owners of voting shares are believed to be unable to coalesce to successfully vote against the wishes of the parent (de facto control).
- Companies acquired (disposed of) are included in (excluded from) consolidation from the date control passes. Also need to consider currently exercisable potential voting rights.
- Czech GAAP** A subsidiary is an enterprise in which the parent ("governing" or "controlling" party) legally exercises either direct or indirect dominant influence.

SUBSIDIARIES (continued)**Special purpose entities (SPE)**

IFRS Requires the consolidation of special purpose entities (SPEs) where the substance of the relationship indicates that an entity controls the SPE, regardless of whether it has a direct or indirect ownership interest in the SPE. Indicators of control arise where:

- the SPE conducts its activities on behalf of the entity; or
- the entity has the decision-making power or other rights to obtain the majority of the benefits of the SPE; or
- the entity has the majority of the residual or ownership risks of the SPE, or of its assets.

Czech GAAP SPEs which are not controlled from the legal point of view, but from which risks and rewards related mainly to the reporting entity should be disclosed in the notes.

Subsidiaries excluded from consolidation

IFRS All subsidiaries are consolidated.

Czech GAAP A subsidiary is excluded from consolidation if: its shares are held exclusively for subsequent re-sale in the immediately following accounting period; significant strict and long-term limitations preventing the parent from exercising its rights relating to the disposal of a subsidiary's assets or its governance or, in rare circumstances, if it may be proven that the cost of obtaining information necessary for consolidation would be inappropriately high.

Certain diversions apply to financial institutions.

Reduction of an interest in a subsidiary

IFRS Under IAS 27, Consolidated and Separate Financial Statements, before revision (2008), the gain or loss on a partial disposal must be calculated by comparing the reduction in the group's interest in the carrying amount of the subsidiary's net assets before and after the disposal, with the proceeds received.

Under the revised IAS 27 (2008), the gain or loss on a partial disposal when control is retained is recorded in equity, because non-controlling shareholders are considered equity providers of the group and transactions among equity providers result in no change in goodwill and no gains or loss. Gain or loss is recognised in the income statement when control is lost as a result of the transaction. In such a case gain or loss is recognised on the ownership interest being disposed (including goodwill allocated to the subsidiary) as well as on the investment retained in the former subsidiary, which is measured at fair value at the date when control is lost.

Czech GAAP No explicit guidance is given on this issue. In practice, companies recognise gain or loss calculated by comparing the reduction in the group's interest in the carrying amount of the subsidiary's net assets before and after the disposal, with the proceeds received.

Uniform accounting policies

IFRS Consolidated financial statements must be prepared using uniform accounting policies for all of the entities in the group.

Czech GAAP Comparable to **IFRS**.

SUBSIDIARIES (continued)**Reporting periods**

- IFRS** Consolidated financial statements of the parent and the subsidiary are usually drawn up as at the same reporting date. However, **IFRS** does permit the consolidation of subsidiary accounts, drawn up as at a different reporting date provided the difference between the reporting dates is not more than three months. Adjustments must be made for significant transactions that occur in the gap period.
- Czech GAAP** Comparable to **IFRS**. The period between the dates on which financial statements subject to consolidation are prepared must not be more than six months for insurance companies.

REFERENCES: IFRS: IAS 27, SIC-12. **Czech GAAP:** Act on Accounting, Decree 500/2000 Coll., Czech accounting standard 020.

INVESTMENTS IN ASSOCIATES**Definition**

- IFRS** An associate is an entity over which the investor has significant influence – that is, the power to participate in, but not control, the associate's financial and operating policies. Participation in the entity's financial and operating policies and/or representation on the entity's board may demonstrate significant influence. A 20% or more interest by an investor in an entity's voting rights leads to a presumption of significant influence.
- Czech GAAP** An associate is an entity over which the parent directly or indirectly exercises significant influence, i.e. holds a minimum 20% and maximum 50% shareholding.

Equity method

- IFRS** An investor must account for an investment in an associate using the equity method. The investor presents its share of the associate's profits and losses in the statement of comprehensive income. **IFRS** further specifies that the associate's results shall be presented at a post-tax level. The investor recognises in equity its share of changes in the associate's equity that have not been recognised in the associate's profit or loss. The investor shall account for the difference, on acquisition of the investment, between the cost of the acquisition and investor's share in fair value of the associate's net identifiable assets, as goodwill. Associate's goodwill is included in the carrying amount of investment.

The investor's investment in the associate is stated at cost, plus share of post-acquisition profits or losses, plus share of post-acquisition movements in equity, less dividends received. Losses that reduce the investment below zero are applied against any long-term interests that, in substance, form part of the investor's net investment in the associate; for example, preference shares or long-term receivables from the associate. Losses recognised in excess of the investor's investment in ordinary shares are allocated to the other components in the net investment in the associate in reverse order of seniority. Further losses are provided for as a liability only to the extent that the investor has got legal or constructive obligation to made payments on behalf of the associate.

Disclosure of information is required about the results, assets and liabilities of significant associates.

INVESTMENTS IN ASSOCIATES (continued)**Equity method (continued)**

Czech GAAP The deemed purchase price allocation as prescribed above for **IFRS** is not performed under **Czech GAAP**. The reporting entity recognises in the consolidated balance sheet its share in the equity of the associate as stated in the associate's books. Goodwill recognised at the date of acquisition is measured as a difference between the consideration paid and the investor's share in the equity of the associate as stated in the associate's books, and is presented together with other goodwill separately from the investment in associate. The investor's share in the associate's profits and losses as determined in the associate's books is always stated at a post-tax level. Financial institutions account for their interests in associates similarly to **IFRS**. **Czech GAAP** requires information about the name and place of registration of the associate, percentage of the shares held by the reporting entity, reporting date of the associate and also names and places of registration of those associates, which have not been accounted for using the equity method, including the reason for such treatment. Furthermore, certain information from the financial statements of the associate itself has to be disclosed.

Impairment

IFRS Impairment is tested as prescribed under IAS 36, Impairment of Assets, if the investment has objective evidence of one of the indicators set out in IAS 39, Financial Instruments: Recognition and Measurement. In estimating future cash flows the investor may use its share of the future net cash flows from the underlying entity, or the cash flows expected to arise from dividends. The investee's goodwill is not subject to impairment testing separately.

Czech GAAP No specific guidance is given on this issue; however, the general requirement to reflect possible asset impairment applies.

INVESTMENTS IN JOINT VENTURES**Definition**

IFRS **IFRS** defines a joint venture as a contractual agreement whereby two or more parties undertake an economic activity that is subject to joint control. Joint control is the contractually agreed sharing of control over an economic activity, and exists only when the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing control (the venturers).

Czech GAAP A joint venture is defined as an entity that is controlled in concert with another party or parties, that are not involved in consolidation, if such parties have the same share in the registered capital of the jointly controlled entity. Joint control must be included in an agreement between parties exercising joint control.

Types of joint ventures

IFRS Distinguishes between three types of joint venture:

- jointly controlled entities, where the arrangement is carried on through a separate entity (company or partnership);
- jointly controlled operations, in which each venturer uses its own assets for a specific project; and
- jointly controlled assets, a project carried on with assets that are jointly owned.

Czech GAAP Types of joint venture are not defined, but only a jointly controlled entity as defined under **IFRS** is considered to be a joint venture.

INVESTMENTS IN JOINT VENTURES (continued)**Jointly controlled entities**

- IFRS** For jointly controlled entities is used either the proportionate consolidation method or the equity accounting method. Proportionate consolidation requires the venturer's share of the assets, liabilities, income and expenses to be combined on a line-by-line basis with the corresponding items in the venturer's financial statements, or to be reported line-by-line as separate line items in the venturer's financial statements.
- Czech GAAP** The proportionate consolidation method has to be applied. In the company (stand alone) financial statements is jointly controlled entity measured at cost or at the investor's share of the jointly controlled entity's equity.

Contributions to a jointly controlled entity

- IFRS** Where a venturer contributes non-monetary assets, such as shares or property, to a jointly controlled entity in exchange for an equity interest in the jointly controlled entity, the venturer must recognise in the statement of comprehensive income the portion of a gain or loss attributable to the equity interests of the other venturers, unless:
- the significant risks and rewards of ownership of the contributed non-monetary asset(s) have not been transferred to the jointly controlled entity; or
 - the gain or loss on the assets contributed cannot be measured reliably; or
 - the contribution transaction lacks commercial substance.

In addition, where the venturer receives assets dissimilar to those it contributed to the jointly controlled entity, the venturer has to recognise an appropriate proportion of the gain in its statement of comprehensive income.

- Czech GAAP** No specific guidance is provided on this issue.

Jointly controlled operations

- IFRS** Jointly controlled operations are similar to jointly controlled entities, but the lack specific incorporated structure. The venturer must recognise in its financial statements: the assets that it controls; the liabilities it incurs; the expenses it incurs; and its share of income from the sale of goods or services by the joint venture.
- Czech GAAP** No specific guidance is given on this issue – this type of joint venture is not defined, in practice it is treated in accounting records similarly to **IFRS**. No specific disclosures are required in the notes.

Jointly controlled assets

- IFRS** The venturer must account for its share in jointly controlled assets; any liabilities it has incurred; any income from the sale or use of its share of the output of the joint venture, together with its share of any expenses incurred by the joint venture and any expenses that it has incurred in respect of its interest in the joint venture.
- Czech GAAP** No specific guidance is given on this issue – this type of joint venture is not defined, in practice it is accounted for according to the legal form of the arrangement.

REFERENCES: IFRS: IAS 1, IAS 28, IAS 31, SIC-13, SIC-20. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll., Czech accounting standard 020.

FOREIGN CURRENCY TRANSLATION

Translation – individual entity

IFRS and **Czech GAAP** have similar requirements regarding the translation of transactions by an individual entity. In **Czech GAAP**, the definition of monetary and non-monetary items does not exist; the accounting treatment is based on specific examples (enumeration), which is different from **IFRS** in its detailed application.

- Translation of transactions denominated in a foreign currency is at the exchange rate valid as at the transaction date.
(**Czech GAAP** specifies that the exchange rate published by the Czech National Bank must be used, or a fixed exchange rate set in advance by the internal guidance of the reporting entity for 12-month period as a maximum; the exchange rate published by the Czech National Bank at the first day of the period for which the fixed exchange rate is used has to be applied. In the case of devaluation or revaluation of the Czech currency, the fixed rate has to be adjusted. Regulated financial institutions are required to use daily rates.)
- Monetary assets and liabilities denominated in a foreign currency are translated at the closing (year-end) exchange rate.
(**Czech GAAP** specifies that the exchange rate published by the Czech National Bank as at the reporting date has to be used.)
- Non-monetary foreign currency assets and liabilities are translated at the appropriate historical acquisition rate.
(**Czech GAAP** requires translation of equity investments acquired in foreign currencies using the Czech National Bank exchange rate at the reporting date.)
- Income statement amounts are translated using historical rates of exchange as at the date of the transactions or at the average rate for the period as a practical alternative. (**Czech GAAP** specifies that the exchange rate published by the Czech National Bank must be used, or the fixed exchange rate set in advance for one reporting period as a maximum; in the case of devaluation or revaluation of the Czech crown the fixed rate must be always changed, the average rate must not be used.)
- Non-monetary items denominated in a foreign currency and carried at fair value are reported using the exchange rate applicable when the fair value was determined (**IFRS**).
- Exchange gains and losses arising on an entity's own foreign currency transactions are reported as part of the profit or loss for the year. This includes long-term loans, which in substance form part of an entity's net investment in a foreign operation. (See page 70 – the hedge of a net investment).

Translation – consolidated financial statements

IFRS requires that where the operations of a foreign consolidated entity are largely independent of the investing (parent) entity's reporting currency, amounts in the foreign entity's statement of financial position be translated using the closing (year-end) rate, with the exception of equity balances, for which the historical rate is used. Amounts in the income statement are usually translated using the average rate for the accounting period. The translation differences arising are reported in equity.

Where a foreign operation is integral to the reporting entity, its individual balances are translated as if all the transactions had been carried out by the reporting entity itself. Under **Czech GAAP**, the statement of financial position and the income statement of a foreign consolidated entity are translated at the rate ruling as at the reporting date. Exchange gains and losses arising from the translation of equity between the opening and the closing statement of financial position of the period also form part of equity of the consolidation group.

FOREIGN CURRENCY TRANSLATION (continued)**Tracking of translation differences in equity**

IFRS These must be tracked separately and the cumulative amounts disclosed. On disposal of a foreign entity (operation), the appropriate amount of cumulative translation difference relating to the entity is transferred to profit or loss and included in the gain or loss on sale.

Czech GAAP No specific guidance is given on this issue.

Translation of goodwill and fair value adjustments on acquisition of foreign entity

IFRS and Czech GAAP Translate at closing rates – goodwill and fair value adjustments are considered to be part of the net assets of the foreign operation.

Foreign entity in hyperinflationary economy

IFRS Restate to current purchasing power prior to translation into the reporting currency of the reporting entity.

Czech GAAP No guidance is given on this issue, since Czech Republic has never been a hyperinflationary economy.

Reporting entity in a hyperinflationary economy

IFRS Where the reporting entity itself reports in the currency of a hyperinflationary economy, the financial statements must be stated in terms of the measuring unit current as at the reporting date.

Czech GAAP No guidance is given on this issue.

REFERENCES: IAS: IAS 21, IAS 29. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll., Czech accounting standard 006 and 020.

BUSINESS COMBINATIONS

Types

A business combination involves the bringing together of separate entities into one economic entity. Two types of business combinations occur in practice. An acquisition is where one of the combining entities obtains control over the other. A group reorganisation can arise from transactions among entities that operate under common control.

IFRS Business combinations among entities, which are not under common control, are always accounted for as acquisitions. Specific **IFRS** guidance about business combinations excludes from its scope transactions among entities under common control and formations of joint ventures (accounting by joint venture entity).

Czech GAAP When accounting for business combinations, a treatment that corresponds to the purchase method is normally used, strictly respecting the legal form of a transaction which often results in a different accounting compared to **IFRS**. In the case of the legal merger or demerger of an entity, Czech legislation also uses the term “company transformations” – individual types of transformations, requirements for the preparation of financial statements, and for valuation of enterprises are specified by the Commercial Code and the relevant accounting regulations and might differ from the **IFRS** treatment.

ACQUISITIONS

Date of acquisition

IFRS The date on which the acquirer obtains control over the acquired entity.

Czech GAAP Comparable to **IFRS**. Often interpreted on the basis of the legal form, i.e. passage of ownership.

Consideration

The consideration transferred in a business combination is the amount of cash or cash equivalents paid, (or fair value of non-monetary assets transferred), liabilities incurred by the acquirer to former owners of the acquiree and equity instruments issued by the acquirer. Where consideration comprises an exchange of shares, specific guidance applies under **IFRS**.

IFRS Shares issued as consideration are recorded at their fair value as at the date of the exchange – the date when the acquirer obtains control over the acquiree’s net assets and operations.

In an active market, the published price of a share at the acquisition date is the best evidence of its fair value.

Czech GAAP No guidance is given on this issue.

Contingent consideration

IFRS If part of the purchase consideration is contingent on a future event, such as achieving certain profit levels, **IFRS** requires an estimate of the amount to be included as part of the cost at the acquisition date. Any revision to the estimate is subsequently recognised in profit or loss. Additional consideration to be paid contingent on the continued employment of a former owner/manager is evaluated based on fact and circumstances as to which part, if any, should be considered as part of the acquisition and which part should be recognised as a separate transaction – employee benefits over the service period.

Czech GAAP No guidance is given on this issue.

ACQUISITIONS (continued)**Acquisition related costs**

- IFRS** Acquisition related costs such as advisory, legal, accounting, valuation and other professional fees and general administrative costs related to the transaction are expensed in the periods in which the costs are incurred.
- Czech GAAP** Acquisition related costs such as advisory, legal, accounting, valuation and other professional fees are capitalised in the consolidated financial statements. General administrative costs are expensed in the periods in which the costs are incurred.

Recognition and measurement of identifiable assets and liabilities acquired

IFRS require separate recognition, by the acquirer, of the acquiree's identifiable assets and liabilities that existed as at the date of acquisition, regardless of whether those identifiable items have been recognised by the acquiree in its accounts. The assets and liabilities must be measured at their fair value as at the date of acquisition.

In **Czech GAAP**, there is no explicit requirement to recognise items, which the acquiree has not previously recognised. In practice, with the exception of goodwill, it is rare to recognise new intangible assets or liabilities as a result of business combination. Furthermore, in business combinations which result in the existence of only one legal entity after the transaction (e.g. mergers or asset deals), the post acquisition carrying amounts of acquired assets and liabilities may not be based on their fair values. Instead, their pre-acquisition book values can be carried over and the related fair value differences are subsumed in so-called "differences arising upon the acquisition". Finally, the two frameworks also apply different criteria to the recognition of restructuring provisions since **Czech GAAP** does not insist on the existence of liability in such case.

Restructuring provisions

- IFRS** The acquirer may recognise restructuring provisions as part of the acquired liabilities only if the acquiree has an existing liability as at the acquisition date for restructuring recognised in accordance with IAS 37, Provision, Contingent Liabilities and Contingent Assets.
- Czech GAAP** No specific rule given on the creation of acquisition provisions, except for financial institutions, where a necessary prerequisite for the creation of a provision is an official irrevocable detailed restructuring plan.

Intangible assets

- IFRS** An intangible asset is recognised separately from goodwill if it represents contractual or legal rights or is capable of being separated or divided and sold, transferred, licensed, rented or exchanged. Acquired in-process research and development (IR&D) is recognised as a separate intangible asset if its fair value can be measured reliably. Non-identifiable intangible assets (e.g. some non-contractual customer relationships) are subsumed in goodwill.
- Czech GAAP** **Czech GAAP** rules for the definition of intangible assets applicable also for assets acquired outside of business combination need to be followed. As a result, less intangible assets are recognised under **Czech GAAP** as a consequence of business combinations.

Minority interests at acquisition

- IFRS** Where an investor acquires less than 100% of a subsidiary, **IFRS** requires the minority interest to be stated at the net fair value of acquired identifiable assets, liabilities and contingent liabilities or at the minority interest's proportional share in the acquired business' fair value. The acquirer has an option to decide, which measurement base it will apply individually for each business combination.

ACQUISITIONS (continued)**Minority interests at acquisition (continued)**

Czech GAAP Minority interests recognised as equity interests must be included in the consolidated financial statements from the date of acquisition. The measurement of minority interest is not explicitly prescribed. In practice, minority interest is measured at the net fair value of acquired identifiable assets, liabilities and contingent liabilities. Minority interest needs to be split among registered capital, retained earnings and other capital funds for presentation purposes.

GOODWILL/CONSOLIDATION DIFFERENCE

Goodwill arises as the difference between the cost of the acquisition and the acquirer's interest in the net fair value of identifiable assets, liabilities and contingent liabilities acquired. It may be positive or negative. Goodwill is capitalised as an intangible asset. When an itemised fair value remeasurement of identifiable assets and liabilities is not performed, the difference is classified under **Czech GAAP** in individual (stand alone) financial statements as "differences arising upon the acquisition" and is presented as part of tangible fixed assets. Negative goodwill or negative "difference arising upon the acquisition" is under **Czech GAAP** presented as an asset with negative carrying amount.

Useful life

IFRS Goodwill is not amortised but reviewed for impairment annually, and when indicators of impairment arise, at the cash-generating-unit level, or group of cash-generating-units level, as applicable.

Czech GAAP Goodwill (in consolidated financial statements labelled as consolidation difference) is amortised on a straight-line basis over the useful life not exceeding 20 years. In individual (standalone) financial statements, the "differences arising upon the acquisition" (when the assets are not remeasured at fair value) are amortised on a straight-line basis over a period of 15 years and goodwill (when assets are remeasured at fair value) over a period of 5 years. For financial institutions the treatment of goodwill is comparable to **IFRS**.

Impairment

IFRS Requires an impairment review of goodwill whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The impairment review does not need to take place at the reporting date. If newly acquired goodwill is allocated to cash-generating-unit that has already been tested for impairment during the period, a further impairment test is required before the reporting date.

The recoverable amount of the cash-generating-unit (i.e., the higher of its fair value less costs to sell and its value in use) is compared to its carrying amount. The impairment loss is recognised in operating results as the excess of the carrying amount over the recoverable amount. Impairment is allocated first to goodwill. Allocation is made on a pro rata basis to the cash-generating-unit's assets if the impairment loss exceeds the carrying amount of goodwill.

Czech GAAP There is no specific guidance that would regulate the requirements and methods of reviewing the impairment of assets. There is only a general requirement to reflect possible impairment but no specific guidance is provided for measurement.

GOODWILL/CONSOLIDATION DIFFERENCE (continued)**Negative goodwill**

- IFRS** If any excess of fair value over the purchase price arises, the acquirer reassesses the identification and measurement of the acquiree's identifiable assets, liabilities and contingent liabilities and the measurement of the cost of the business combination. Any excess remaining after reassessment is recognised immediately in the statement of comprehensive income.
- Czech GAAP** Negative goodwill is treated in the same way as positive goodwill. The presentation of "negative consolidation difference" is not addressed in the guidance for preparation of consolidated financial statements.

SUBSEQUENT ADJUSTMENT TO ASSETS AND LIABILITIES

- IFRS** Permits within the so-called "measurement period" adjustments to original fair values recognised at acquisition as additional evidence becomes available to measure those values. Subsequent adjustments can only be performed as a correction of error.
- Czech GAAP** No specific standard for subsequent adjustment to assets and liabilities. On acquisition of a set of assets, the acquirer may subsequently remeasure individual assets based on an expert's valuation and adjust carrying amounts accordingly. However, if the acquisition is performed within three months before the reporting date, the remeasurement may also be performed in the subsequent period.

DISCLOSURE

ITEM	IFRS	Czech GAAP
General		
Names and descriptions of the combining entities	Mandatory	Mandatory
The effective date of the combination for accounting purposes	Mandatory	Mandatory
The cost of acquisition and the form of the consideration given, including any deferred and contingent consideration	Mandatory	Not required
Operations to be disposed of	Mandatory	Not required
The % of voting shares acquired	Mandatory	Not required
Goodwill		
Total amount of goodwill - the reasons for the acquisition, including a description of the factors that led to a purchase price that resulted in goodwill	Mandatory	Not required
Goodwill – method & amortisation period	Not applicable	Mandatory
Goodwill – impairment charge	Mandatory	Not required
Reconciliation of the goodwill between opening and closing amount	Mandatory	Not required
Other financial disclosures		
Summary of fair value of assets and liabilities acquired with separate disclosure of cash equivalents	Mandatory	Not required
Effect of acquisition on the financial position as at the reporting date and on the results since the acquisition	Mandatory	Not required
If the acquisition accounting had not been finalised, disclose that fact and the reasons. In subsequent periods, adjustments made to the initial allocations must be disclosed.	Mandatory	Not required
For a series of individually immaterial business combinations that are material in the aggregate: <ul style="list-style-type: none"> • the number of entities and brief description • the aggregate cost, the number and value of equity instruments issued or to be issued • aggregate amount of any contingent payments, options or commitments 	Mandatory	Not required

COMMON CONTROL TRANSACTIONS

IFRS Does not specifically address such transactions. Entities should develop and consistently apply an accounting policy; management can elect to apply purchase accounting or the predecessor amounts method to a business combination involving entities under common control. The accounting policy can be changed only when the criteria in IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors, are met. Related party disclosures are used to explain the impact of transactions with related parties on the financial statements.

Czech GAAP This issue is not addressed. In practice, it is treated as if no common control exists.

REFERENCES: IFRS: IFRS 3R, IAS 12. Czech GAAP: Act on Accounting, Decree 500/2002 Coll., Czech accounting standard 020.

REVENUE RECOGNITION

Definition

IFRS Income under **IFRS** embraces both revenue and gains. The standard IAS 18, Revenues on revenue recognition defines revenue as the gross inflow of economic benefits during the reporting period arising from the ordinary activities of an enterprise when the inflows result in an increase in equity, other than increases relating to contributions from equity participants.

Czech GAAP There is no well-developed definition of revenue and frequently the legal form of a transaction is followed. Revenue is recognised at the date when goods are delivered to a buyer or when service is rendered.

Measurement

IFRS requires measurement of revenues at the fair value of the consideration received or receivable. This is usually the amount of cash or cash equivalents received or receivable. In practice, the treatment under **Czech GAAP** is often consistent with **IFRS**. Where the inflow of cash or cash equivalents is deferred, discounting to a present value is required under **IFRS**. Except for arrangements with interest stipulated in a contract, discounting to the present value is not permitted under **Czech GAAP**.

Revenue recognition

IFRS IAS 18 describes specific revenue recognition criteria for the sale of goods and for the rendering of services and interest, royalties and dividends. The revenue recognition criteria common to each of these are the probability that the economic benefits associated with the transaction will flow to the entity and that the revenue and related costs can be measured reliably.

Additional recognition criteria apply to revenue arising from the sale of goods. **IFRS** requires that the seller has transferred the significant risks and rewards of ownership of the goods to the buyer and retains no control over the goods. Revenue from the rendering of services must be recognised by reference to the state of completion of the transaction at the reporting date. Interest income must be recognised on a basis that takes into account the asset's effective yield (interest rate). Royalties are recognised on an accrual basis and dividends are recognised when the shareholder's right to receive payment is established.

Czech GAAP Concentrates on formal aspects of the transaction and does not require explicitly reliable determination of related expenses. Revenue which relates to a different accounting period is deferred or accrued in the balance sheet (rentals, insurance premiums, etc.). The effective interest method is only required in the case of financial institutions for financial instruments measured at amortised cost; in other cases it is not specifically addressed and straight-line recognition is usually applied.

Revenue recognition criteria for sale of goods

IFRS

- it is probable that economic benefits will flow to the entity,
- the entity has transferred to the buyer the significant risks and rewards of ownership of the goods,
- the amount of revenue can be measured reliably,
- the entity retains no effective control over the goods,
- the costs incurred or to be incurred in respect of the transaction can be measured reliably and,
- the stage of completion of the transaction can be measured reliably.

REVENUE RECOGNITION (continued)

Revenue recognition criteria for sale of goods (continued)

Czech GAAP does not stipulate comparable criteria and the form of a transaction is often decisive, which in the case of a number of non-standard transactions may cause practical problems.

SPECIFIC REVENUE RECOGNITION ISSUES

Warranty and product maintenance contracts

IFRS When a product's selling price includes an identifiable component for subsequent servicing, the related amount is deferred and recognised over the period during which the service is performed. For standard warranty obligations, provisions are created in accordance with IAS 37. Warranty costs form part of the cost of sales.

Czech GAAP Not addressed specifically; in practice, provisions are often created for warranty repairs, but may also be created for future servicing commitments. There is no guidance for distinguishing between normal warranty provisions and servicing arrangements beyond standard warranty.

Barter transactions - advertising

An advertising barter arrangement exists when two companies enter into a non-cash transaction to exchange advertising services.

IFRS Under **IFRS**, revenue may be recognised on the exchange of dissimilar goods and services if the amount of revenue can be measured reliably. The transaction must be measured at the fair value of goods or services received, adjusted by the amount of any cash or cash equivalents transferred; however, where the fair value of goods or services received cannot be measured reliably, the fair value of the goods and services given up, adjusted by the amount of any cash or cash equivalents is used. The fair value of advertising received or provided in a barter transaction is generally measured by reference to equivalent non-barter (i.e. cash) transactions.

Czech GAAP No guidance is given on this matter.

CONSTRUCTION CONTRACTS

Scope

IFRS Guidance applies to fixed-price and cost-plus construction contracts of contractors (not defined), for the construction of a single asset or combination of assets.

Czech GAAP No special accounting guidance for construction contracts exists.

Recognition method

IFRS The recognition of revenue and expenses by reference to the stage of completion of a contract (referred to as the percentage of completion method) is applied if the outcome can be measured reliably. The criteria necessary for a cost-plus contract to satisfy reliable measurement are less restrictive than for a fixed-price contract. When the final outcome cannot be estimated reliably, **IFRS** requires the use of the zero-profit method, which recognises revenue only to the extent of contract costs incurred that are expected to be recovered. **IFRS** provides limited guidance is given on the use of estimates. The completed contract method is not permitted.

CONSTRUCTION CONTRACTS (continued)**Recognition method (continued)**

Czech GAAP The percentage of completion method is not provided for in **Czech GAAP**. Accounting treatment is dependent on the terms of the contract, it usually has the form of the completed contract method and in the case of work in progress, supplies are usually stated at direct cost, production and administrative overheads. If there is partial invoicing agreed in the contract, the revenue and related costs are recognised in the income statement based on invoicing. If progress payments are agreed in the form of advance payments, advances paid by customers on long-term contracts before the fulfilment of the commitment to the customer are recorded as a liability with revenue, costs and profit on the project deferred until its completion. Anticipated losses should be recognised and provided for earlier, in the period when ascertained.

Applying the percentage of completion method

IFRS When the outcome of the contract can be estimated reliably, revenue and costs must be recognised by reference to the stage of completion of the contract activity as at the reporting date. When it is probable that total contract costs will exceed total contract revenue, the expected loss must be recognised as an expense immediately.

Czech GAAP Not relevant; in the case of anticipated loss a provision for work in progress needs to be created. The manner of its calculation is not prescribed.

Completed contract method

IFRS Prohibited.

Czech GAAP Depends on the form of contractual arrangement. In practice this method is mostly applied.

Combining contracts and segmenting a contract

IFRS Requires that contracts be combined when part of a package, or segregated when each contract is part of a separate proposal; each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract related to each asset and when revenues and costs for each segment can be clearly identified.

Czech GAAP No guidance is given on this matter.

REFERENCES: IFRS: IAS 11, IAS 18, **Czech GAAP** – Act on Accounting, Decree 500/2002 Coll., Czech accounting standards 019 and 015.

EXPENSE RECOGNITION

Definition

IFRS Expenses are defined in the **IFRS** Framework to include losses. Expenses are decreases in economic benefits that result in a decrease in equity.

Czech GAAP No specific definition of expenses exists.

SPECIFIC EXPENSE RECOGNITION ISSUES

INTEREST EXPENSE

IFRS Interest expense is recognised on an accrual basis. Where interest expense includes a discount or premium arising on the issue of a debt instrument, the discount or premium is amortised using the effective interest rate method. The effective interest rate is the rate that discounts the estimated future cash payments through the expected life of the debt instrument to the carrying amount of the debt instrument.

Czech GAAP Interest expense is recognised on an accrual basis with reference to the debt instrument contractual interest rate. Financial institutions use mandatorily effective interest rate in cases described by the Decree; however, they may apply the straight-line rate for current liabilities and other payables settled by regular instalments.

EMPLOYEE BENEFITS - PENSIONS

IFRS Requires that the cost of providing these benefits be recognised on a systematic and rational basis over the period during which employees provide services to the entity. Separates pension plans into defined contribution plans and defined benefit plans.

Czech GAAP Currently, no specific guidance (standard) on this matter is available under **Czech GAAP**. There is a state pension system with possible supplementary pension schemes (contributory pension plans) run by private pension funds. Business companies contribute to the state pension system and can possibly also contribute on behalf of their employees to the private pension funds.

Defined contribution plans

Defined contribution plans are post-employment benefit plans that require the entity to pay fixed contributions into a fund. The entity is under no legal or constructive obligation to make further contributions to the fund even if losses are sustained. Under these plans it is the employee who is exposed to the risk attributable to the plan assets. **IFRS** requires that the pension cost be measured as the contribution payable to the fund on a periodic basis.

Defined benefit plans

Defined benefit plans oblige the employer to provide defined post-employment benefits of set amounts to employees. The risks associated with plan assets rest with the employer.

Czech GAAP So far, it is not common practice in the Czech Republic for employers to have defined benefit plans and no guidance is given on such plans is available under **Czech GAAP**, however, provision for liabilities resulting from such plans should be recognised using the general principles of **Czech GAAP**. Defined contribution plans are recorded in accordance with **IFRS**.

EMPLOYEE BENEFITS – PENSIONS (continued)**Defined benefit plans (continued)**

The key features of the methodology for accounting for defined benefit plans under IFRS are:

ITEM	IFRS
Determination of pension and post-retirement expense	Projected unit credit actuarial method used.
Discount rate for obligations	Based on market yields for high quality corporate bonds. Government bond yields should be used when there is no deep market in high quality corporate bonds.
Valuation of plan assets	Measure at fair value or using discounted cash flows if market prices unavailable. Insurance contracts measured at fair value. Where plan assets include qualifying insurance policies that exactly match the amount and timing of some or all of the benefits payable under the plan, the fair value of those insurance policies is deemed to be the present value of the related obligations.
Recognition of actuarial gains and losses	Immediate recognition and amortisation over expected remaining working lives of participating employees. At a minimum, a net gain/loss in excess of 10% of greater of defined benefit obligation or actual (fair) value of plan assets at beginning of year must be recognised. An entity can adopt a policy of recognising actuarial gains and losses in full in the period in which they occur and recognition may be outside of profit or loss. Amounts recognised directly in the statement of comprehensive income are not subsequently reclassified into profit or loss.
Expected return on plan assets	Based on market expectations at the beginning of the period for returns over the entire life of the related obligation. Reflects changes in the fair value of plan assets as a result of actual contributions and benefits paid. The rate is applied to the fair value of plan assets.
Statement of financial position asset limitation	An asset limited to the lower of: a) the asset resulting from applying the standard, and b) the net total of any unrecognised actuarial losses and past service cost and the present value of any available refunds from the plan or reduction in future contributions to the plan.
Past-service cost	Positive and negative past-service cost recognised over remaining vesting period. Where benefits have already vested, recognise past-service cost immediately.
Multi-employer plans	Use defined benefit accounting unless sufficient information available. If there is a contractual agreement between the multi-employer plan and its participants, and the plan is accounted for as a defined contribution plan, the asset or liability that arises from the contractual agreement and the resulting income or expense in profit or loss are recognised.
Subsidiary's defined benefit pension plan forming part of a group plan	Plans with participating entities under common control are not multi-employer plans. If there is a contractual arrangement between the subsidiary and the parent, the subsidiary accounts for the benefit costs on that basis; otherwise the contribution payable for the period is recognised as an expense, except for the sponsoring employer, which must apply defined benefit accounting for the plan as a whole.
Curtailement definition	A curtailment occurs either when an entity is demonstrably committed to making a material reduction in the number of employees covered by the plan or when it amends the terms of the plan such that a material element of future service by current employees will no longer qualify for benefits, or will qualify only for reduced benefits.

EMPLOYEE BENEFITS – PENSIONS (continued)**Defined benefit plans (continued)**

ITEM	IFRS
Settlement definition	A settlement occurs when an entity enters into a transaction that eliminates all further legal or constructive obligation for part or all the benefits under the plan.
Curtailement/settlement (timing of recognition)	Gains and losses are recognised when curtailments/settlements occur.
Curtailement/settlement (calculation of gains and losses)	Gains and losses on curtailments/settlements include changes in the present value of the defined benefit obligation, any resulting changes in the fair value of the plan assets and any related actuarial gains and losses and past-service cost that had not previously been recognised.

REFERENCES: IFRS: IAS 19, IAS 39.

SHARE BASED PAYMENTS**Recognition**

IFRS Shares and share options are sometime granted to employees as part of their remuneration package or to other third parties in exchange for goods or services. The goods or services acquired in a share-based transaction are recognised. The fair value of shares and options awarded to employees is recognised over the period to which the employees' services relate. The award is presumed to be for past services if it is unconditional without any performance criteria.

The credit side of the entry is a liability if the entity has an obligation to settle the transaction in cash. However, the credit entry is an increase in equity if there is no obligation to settle in cash; the consideration for goods and services will therefore be achieved through the issuance of equity instruments. If the fair value of the goods or services exceeds the fair value of the obligation to settle in cash, the credit entry will comprise both a liability and an increase in equity.

Czech GAAP No guidance is given on this matter.

Measurement

IFRS For equity-settled share-based payment transactions, the goods or services received and the corresponding increase in equity are measured at the fair value of the goods or services received. If the entity cannot reliably estimate the fair value of the goods or services received, as will be the case with employee services, it should measure their value and the corresponding increase in equity by reference to the fair value of the equity instruments granted. For cash-settled share-based payment transactions, the goods or services acquired and the liability incurred are measured at the fair value of the liability. Extensive disclosures are also required.

Czech GAAP No guidance is given on this matter.

Employer's payroll tax payable on exercise of share options by employee

IFRS Employers' social security liability arising from share-based payment transactions is recognised over the same period as the share-based payment charge.

Czech GAAP No guidance is given on this matter.

SHARE BASED PAYMENTS (continued)

Non-employee share-based payment transactions

IFRS **IFRS 2** requires the fair value of the goods or services acquired by an entity to be determined and used as the value of an equity-settled share-based payment transaction. There is a rebuttable presumption that the fair value of the goods and services can be reliably estimated. However, where the identifiable fair value of the goods or services received is less than the fair value of the equity instruments issued, there is a presumption that unidentifiable goods or services have also been received. Identifiable goods or services acquired in a share-based payment transaction are recognised when they are received. Unidentifiable goods or services are measured at fair value as at the grant date.

Czech GAAP No guidance is given on this matter.

REFERENCES: IFRS: IAS 19, IAS 37, IFRS 2.

COMPENSATED ABSENCES

Includes long-term compensated absences such as long-term disability, long service and holidays. These benefits typically accumulate over the employee's service period. **IFRS** requires that the liability be recognised, as the employee provides the service that gives rise to the right to the benefit. Under **Czech GAAP**, in practice a provision for untaken holidays is recorded using the general liability recognition principles.

TERMINATION BENEFITS

IFRS Termination benefits arising from redundancies are accounted for in a similar way to restructuring provisions. In the event of an offer made to encourage voluntary redundancy, the measurement of termination benefits should be based on the number of employees expected to accept the offer.

Termination indemnities are generally payable regardless of the reason for the employee's departure. The payment of such benefits is certain (subject to any vesting or minimum service requirements) but the timing of their payment is uncertain. **IFRS** requires that termination indemnities be accounted for consistently with pension obligations (i.e., including expected salary progression element).

Czech GAAP It is recorded as a component of the restructuring provision.

REFERENCES: IFRS: IAS 19. Czech GAAP: Czech accounting standard 004.

ASSETS**INTANGIBLE ASSETS****Definition**

IFRS An identifiable non-monetary asset without physical substance. May be acquired or internally generated.

Czech GAAP There are specifically defined assets that are classified as intangible assets – establishment costs, research and development, software, royalties (for instance know-how and licences) and goodwill with a useful life longer than one year.

Recognition – acquired intangibles ⁽ⁱ⁾

IFRS General **IFRS** asset recognition criteria apply. Recognise if future economic benefits attributable to the asset are probable and the cost of the asset can be measured reliably.

Czech GAAP Intangible assets are capitalised and amortised if they are consistent with the defined examples of intangible assets, their cost is higher than the amount determined by the internal company guidance and their anticipated useful life is longer than one year. Since 2009, establishment costs of financial institutions including balances brought forward from the past need to be expensed immediately.

(i) For accounting of intangible assets acquired in a business combination see the chapter Business combinations (page 32).

Recognition – additional criteria for internally generated intangibles

IFRS Requires distinguishing costs associated with the creation of intangible assets between the research phase and the development phase. Costs in the research phase must always be expensed. Costs in the development phase are expensed unless the entity can demonstrate all of the following:

- the technical feasibility of completing the intangible asset,
- the intention to complete the intangible asset,
- the ability to use or sell the intangible asset,
- how the intangible asset will generate future economic benefits. The entity must demonstrate the existence of a market or, if for internal use, the usefulness of the intangible asset,
- the availability of adequate resources to complete the development and to use or sell the intangible asset,
- the ability to measure reliably the expenditure attributable to the intangible asset during its development.

Development costs initially recognised as an expense cannot be capitalised in a subsequent period.

Czech GAAP Internally generated intangible assets for own use are not capitalised. Development costs for assets held-for-sale are capitalised.

Recognition – website development costs (website)

IFRS Costs incurred during the planning stage must be expensed. Costs incurred for activities during the website's application and infrastructure development stages must be capitalised. Costs incurred during the content development stage and costs incurred during the operation stage must be expensed as incurred.

Czech GAAP No guidance is given on this matter. The general rule that costs incurred when generating intangible assets internally for own use are expensed applies.

INTANGIBLE ASSETS (continued)**Measurement – acquired intangibles**

IFRS The cost of a separately acquired intangible asset as at the date of acquisition is usually self-evident, being the fair value of the consideration paid.

Czech GAAP Comparable to **IFRS** – acquired intangible assets are measured at cost, including incidental attributable costs.

Measurement – internally generated intangibles

IFRS The cost comprises all expenses that can be directly attributed or allocated to creating, producing and preparing the asset from the date when the recognition criteria are met.

Czech GAAP Initially measured at cost, which corresponds to directly attributed or allocated expenses related to development of the intangible asset.

Subsequent measurement – acquired and internally generated intangibles

IFRS Intangible assets are measured at cost less accumulated amortisation/impairment. Subsequent revaluation of intangible assets to their fair value must be based on prices in an active market. Where an entity adopts this treatment (extremely rare in practice), the revaluations must be regularly performed and a revaluation of the entire class of intangible assets must take place at the same time.

Czech GAAP Intangible assets are carried at cost or at cost less accumulated amortisation. Fair value remeasurement is not permitted.

Amortisation – acquired intangibles

IFRS Amortised if the asset has a finite life; not amortised if the asset has an indefinite life, but should be tested at least annually for impairment. There is no presumed maximum life.

Czech GAAP Amortised gradually over the asset's useful life based on the depreciation plan. All intangible assets have to be amortised.

Impairment – acquired and internally generated intangibles

IFRS Impairment reviews are required whenever changes in events or circumstances indicate that an intangible asset's carrying amount may not be recoverable. Annual reviews are required for intangible assets with indefinite useful lives and for assets not yet ready for use. Assets with indefinite useful lives are usually reviewed for impairment as part of a cash-generating unit (CGU). Reversals of impairment losses are allowed under specific circumstances.

Czech GAAP Impairment is reflected either by a provision or an extraordinary write-off of an asset; no specific guidance is available for determining the impairment loss.

REFERENCES: IFRS: IAS 36, IAS 38, SIC-32. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll., Czech accounting standards 005 and 013.

PROPERTY, PLANT AND EQUIPMENT

Definition

IFRS PPE are tangible assets that are held by an entity for: (i) use in the production or supply of goods or services; (ii) rental to others; or (iii) administrative purposes.

Czech GAAP There are specifically defined assets that are classified as tangible fixed assets (equivalent category to PPE), basically comparable to **IFRS**, except for assets acquired under finance lease contracts and a separate category of differences arising upon the acquisition (of assets).

Recognition

IFRS General **IFRS** asset recognition criteria apply. Recognise if future economic benefits attributable to the asset are probable and the cost of the asset can be measured reliably.

Czech GAAP Tangible fixed assets (PPE) are capitalised if their cost is higher than the price determined by the entity and they have an anticipated useful life longer than one year. Economic benefits are not a criterion for asset recognition.

Initial measurement

IFRS Comprises the costs directly attributable to the asset's acquisition and transport to the location and working conditions necessary for it to be capable of operating in the way management intends and includes costs of testing whether the asset is functioning properly. Start-up and pre-production costs must not be capitalised unless they are a necessary part of bringing the asset to its working condition. The following are also included in the initial measurement of an asset:

- the costs of site preparation
- initial delivery and handling costs
- installation and assembly costs
- costs of employee benefits arising from construction or acquisition of the asset
- costs of testing whether the asset is functioning properly
- professional fees
- fair value gains/losses on qualifying cash flow hedges relating to the purchase of PPE in a foreign currency (see page 70).
- borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset (see page 51).

Government grants received in connection with acquisition of PPE may be offset against the cost or recognised separately (see page 64).

Czech GAAP Similar to **IFRS**, recognises costs directly attributable to the asset acquisition. However, dismantling costs, asset removal expenses and the costs of resuming the site's original conditions are not included in the asset's initial measurement. Interest expense (borrowing costs) for tangible assets in the course of construction are capitalised, should an entity decide to do so. After inception into use, capitalised interest is amortised over the asset's useful life.

Subsequent expenditure

IFRS Subsequent maintenance expenditure is expensed as incurred. Replacement of parts can be capitalised when specific criteria are met. The cost of a major inspection or overhaul occurring at regular intervals is capitalised where the recognition criteria applicable to PPE are satisfied. The net book value of any replaced component would be expensed at the time of overhaul.

PROPERTY, PLANT AND EQUIPMENT (continued)**Subsequent expenditure (continued)**

Czech GAAP PPE carrying amount is increased by so-called property enhancements (technical improvements), if aggregate expenses for the period exceed the amount stipulated by the Income Taxes Act (i.e. from 2007: CZK 40,000).

Depreciation

IFRS The depreciable amount of an item of PPE must be allocated on a systematic basis over its useful life, reflecting the pattern in which the entity consumes the asset's benefits. Any change in the depreciation method used is treated as a change in an accounting estimate being reflected in the depreciation charge for the current and future periods. The depreciation methods are reviewed periodically; residual values and useful lives are reviewed as at each reporting date. If PPE item consists of components with different useful lives, each component needs to be depreciated separately over its useful life.

Czech GAAP Comparable to **IFRS**. Component approach can be applied from 1 January 2010 as a policy choice.

Subsequent measurement

IFRS The benchmark treatment requires that an asset be carried at cost less accumulated depreciation and impairment. However, revaluation of PPE at fair value is permitted under the alternative treatment.

The revaluation model should be applied to an entire class of assets.

The increase of an asset's carrying amount as a result of a revaluation must be credited directly to equity under the heading "revaluation surplus", unless it reverses a revaluation decrease for the same asset, previously recognised as an expense; then it must be recognised as income in profit or loss. A revaluation decrease must be charged directly against any related revaluation surplus for the same asset, with any excess being recognised as an expense.

Disclosure of the historical cost equivalent (cost and accumulated depreciation) of assets carried at revalued amounts (fair value) is required.

Czech GAAP Revaluation not permitted, recognised at cost less accumulated depreciation and impairment.

Frequency of revaluations

IFRS Revaluations must be kept sufficiently up to date so that the carrying amount does not differ materially from the fair value. This requires regular revaluations of all PPE when the revaluation policy is adopted. Management must consider as at each year end whether the fair value is materially different from the carrying amount.

Czech GAAP Not applicable.

PROPERTY, PLANT AND EQUIPMENT (continued)**Impairment of revalued PPE**

IFRS An impairment loss (downward revaluation) may be offset against revaluation surpluses to the extent that it relates to the same asset; any uncovered deficit in excess of the existing revaluation surpluses must be recognised in profit or loss for the period.

Czech GAAP All impairments are recognised in the income statement.

REFERENCES: IFRS: IAS 16, IAS 23, IAS 36, SIC-23. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll., Czech accounting standards 005 and 013.

NON-CURRENT ASSETS HELD FOR SALE

IFRS A non-current asset is classified as held-for-sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. The asset should be available for immediate sale in its present condition, and its sale should be highly probable. For the sale to be highly probable, the appropriate level of management should be committed to a plan to sell the asset, and an active programme to locate a buyer and complete the plan should have been initiated. The asset should be actively marketed for sale at a price that is reasonable in relation to its current fair value. The sale should be expected to qualify for recognition as a completed sale within one year from the date of classification, and actions required to complete the plan should indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn. Once classified as held for sale, the asset is measured at the lower of its carrying amount and fair value less costs to sell.

Czech GAAP No similar category exists. Fixed tangible and intangible assets are presented as non-current assets until their disposal. Depreciation or amortisation continues until disposal.

REFERENCES: IFRS: IFRS 5. **Czech GAAP:** Czech accounting standard 013.

LEASES

Classification

While substance rather than legal form is applied under **IFRS**, definite form-driven approach is stipulated in the **Czech GAAP**.

A finance (capital) lease exists under **IFRS** if the agreement transfers substantially all the risks and rewards associated with ownership of the asset to the lessee. **IFRS** provides certain indicators for determining the classification of a lease. These are presented below.

INDICATOR	IFRS
Normally leads to a finance lease	
Ownership is transferred to the lessee at the end of the lease term	Indicator of a finance lease
A bargain purchase option exists	Indicator of a finance lease
The lease term is for the majority of the leased asset's economic life	Indicator of a finance lease
The present value of minimum lease payments is equal to substantially all the fair value of the leased asset	Indicator of a finance lease
The leased assets are of a specialised nature such that only the lessee can use them without major modification	Indicator of a finance lease
Could lead to a finance lease	
On cancellation, the lessor's losses are borne by the lessee	Indicator of a finance lease
Gains and losses from the fluctuation in the fair value of the residual fall to the lessee	Indicator of a finance lease
The lessee has the ability to continue the lease for a secondary period at below market rental	Indicator of a finance lease

Under **Czech GAAP**, the transfer of ownership at the end of the lease term must be agreed for a finance lease. However, the classification of lease arrangement is not important for financial reporting purposes, because both finance and operating leases are treated in the same way under **Czech GAAP**.

Recognition of the investment in the lease

IFRS: The amount due from a lessee under a finance lease is to be recognised as a receivable at the amount of the net investment in the lease. At any point in time, this will comprise the total of the future minimum lease payments less gross earnings allocated to future periods. Minimum lease payments for a lessor include guarantees from a third party related to the leased assets under **IFRS**. The present value of minimum lease payments would generally use the implicit rate in the lease for discounting under **IFRS**.

The lessor's gross earnings are allocated between the receipt of the capital amount (principal) and receipt of finance income (interest) to provide a constant rate of return. **IFRS** requires the use of the net investment method to allocate gross earnings, which excludes the effect of cash flows arising from taxes and financing related to the lease transaction.

Under **Czech GAAP**, the fact that the lessee controls the asset is not reflected. The method of accounting for finance and operating leases is the same. The asset is recorded in the lessor's balance sheet as PPE.

LEASES (continued)**Operating leases**

Both frameworks require an asset leased under an operating lease to be recognised by the lessor as PPE and depreciated over its useful life. Rental income is generally recognised on a straight-line basis over the lease term.

Incentives

IFRS requires that the lessor recognise the aggregate cost of incentives given as a reduction of rental income over the lease term on a straight-line basis, unless another systematic basis is more representative of the time pattern over which the benefit of the leased asset is diminished.

This issue is not specifically addressed by **Czech GAAP**; in practice the treatment under **IFRS** is used.

REFERENCES: IFRS: IAS 17. **Czech GAAP:** Decree 500/2002 Coll., Czech accounting standard 013.

IMPAIRMENT OF ASSETS**Recognition**

IFRS An entity must assess as at each reporting date whether there are any indications that an asset may be impaired. If there is any such indication, the assets must be tested for impairment. An impairment loss must be recognised in profit or loss when an asset's carrying amount exceeds its recoverable amount. Assets classified as held-for-sale are measured at the lower of the carrying amount and fair values less costs to sell.

Czech GAAP There is only a general requirement to reflect possible impairment. No detailed guidance for the measurement is provided. Permanent and temporary impairment are distinguished. Permanent impairment leads to direct write-off of an asset, provision is created for temporary impairment, however, in practise most impairments are treated as temporary.

Measurement

IFRS The impairment loss is the difference between the asset's carrying amount and its recoverable amount. The recoverable amount is the higher of the asset's fair value less cost to sell and its value in use. Value in use is the future cash flows to be derived from the particular asset, discounted to present value using a pre-tax market-determined rate that reflects the current assessment of the time value of money and the risks specific to the asset.

Czech GAAP No guidance is given on this matter.

Reversal of impairment loss

IFRS Requires reversal of impairment losses when there has been a change in economic conditions or in the expected use of the asset.

Czech GAAP No specific guidance is given on this matter – however, reversal of the provision due to temporary impairment of an asset's value through the income statement is permitted (basically comparable to **IFRS**).

REFERENCES: IFRS: IAS 16, IAS 36. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll., Czech accounting standard 005.

CAPITALISATION OF BORROWING COSTS

Recognition

- IFRS** Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are required to be capitalised as part of the cost of that asset. A qualifying asset is one that necessarily takes a substantial period of time to get ready for its intended use or sale.
- Czech GAAP** Under **Czech GAAP**, borrowing costs are capitalised or expensed depending on the entity specific accounting policy. After commissioning of the assets and commencement of their use, borrowing costs included in the cost of the asset and amortised over its estimated useful life.

Measurement

- IFRS** The amount of interest eligible for capitalisation is either the actual cost incurred on a specific borrowing or an amount calculated using the weighted average method, considering all the general borrowings outstanding during the period for that entity. Interest can include foreign exchange differences, but under tightly defined conditions. Any interest earned on the temporary investment of funds borrowed to finance the asset's production is netted with the interest expense to be capitalised. Capitalisation of interest must cease once the asset is ready for its intended use or sale.
- Czech GAAP** Not specified, but only the contractual interest can be capitalised, not other borrowing costs (transaction costs of the debt instrument, discounts, fees, etc.). When funds are borrowed generally, the reporting entity may not capitalise interest expense from the general funds even when its accounting policy is to capitalise directly attributable interest expenses.

REFERENCES: IAS: IAS 23. **Czech GAAP:** Decree 500/2002 Coll.

INVESTMENT PROPERTY

Definition

- IFRS** Property (land and buildings) held in order to earn rentals and/or for capital appreciation. Does not include owner-occupied property or property held for sale.
- Czech GAAP** Not specifically defined, guidance is given on PPE should be followed.

Initial measurement

- IFRS** Requires the same cost-based measurement for both acquired and self-constructed investment property. The cost of a purchased investment property comprises its purchase price and any directly attributable costs such as professional fees for legal services, property transfer taxes and other transaction costs. Self-constructed property shall be initially measured at cost until its fair value is reliably determinable, if the reporting entity applies the fair value model (see subsequent measurement below). Property held under a finance or operating lease can also be classified as investment property.
- Czech GAAP** No specific guidance is given on this matter. These assets are classified as PPE (see page 47).

INVESTMENT PROPERTY (continued)**Subsequent measurement**

IFRS The entity can choose between the fair value model or cost model for all investment property. When fair value is applied, the gain or loss arising from a change in the fair value is recognised in profit or loss for the period in which it arose and the carrying amount is not depreciated.

Czech GAAP No specific guidance is given on this matter. The rules (policies) for measurement of PPE apply (cost less depreciation), fair value measurement is not allowed.

Transfers to/from investment property

IFRS When there is a change in use of the investment property, the standard provides a detailed guidance for subsequent classification. Investment property to be sold is re-classified as inventories, and investment property to be owner-occupied is reclassified as PPE.

Czech GAAP Not applicable – no transfers could arise.

Frequency and basis of revaluations

IFRS The fair value of investment property must reflect the actual market conditions and circumstances as at the reporting date. The standard does not require use of an independent and qualified valuer, but it is encouraged. Fair value is based on the so-called highest and best use concept. Revaluations must be made with sufficient regularity that the carrying amount does not differ materially from fair value.

Czech GAAP Not applicable.

REFERENCES: IFRS: IAS 40.

INVENTORIES**Definition**

Both frameworks define inventories as assets that are: held for sale in the ordinary course of business; in the process of production for such sale; or in the form of materials or supplies to be consumed in the production process or in rendering services.

Measurement

IFRS Carried at the lower of cost or net realisable value (sale proceeds less all further costs to bring the inventories to completion). Reversal (limited to the amount of the original write-down) is required for a subsequent increase in value of inventory previously written down.

Czech GAAP Basically comparable to **IFRS**, however, no guidance for the measurement of potential decrease in value.

INVENTORIES (continued)**Formula for determining cost**

Method	IFRS	Czech GAAP
LIFO	X	X
FIFO	✓	✓
Weighted average cost	✓	✓

✓ Permitted

X Prohibited

Consistency of the cost formula for similar inventories

IFRS Requires that an entity use the same cost formula for all inventories that have a similar nature and use to the entity.

Czech GAAP Comparable to **IFRS**.

Allocation of fixed overheads

IFRS Any allocation of fixed production overheads is based on normal capacity levels, with unallocated overheads expensed as incurred.

Czech GAAP Basically comparable to **IFRS**, but no detailed requirements. In the case of bulk production with a short production cycle, production overheads are not capitalised.

REFERENCES: IAS: IAS 2. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll., Czech accounting standard 015.

BIOLOGICAL ASSETS

Under **IFRS** a biological asset should be measured on initial recognition and as at each reporting date at its fair value less estimated point-of-sale costs. All changes in fair value should be recognised in profit or loss in the period in which they arise. Under **Czech GAAP** no specific guidance is given on this matter except for arbitrary rules specifying which animals should be treated as inventories and as PPE, general treatment for inventories or PPE applies, i.e. fair value in excess of cost cannot be used.

REFERENCES: IAS: IAS 41. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll.

FINANCIAL ASSETS

IFRS **IFRS** outlines the recognition and measurement criteria for all financial assets, defined to include derivatives.

Czech GAAP The guidance in this area has been broadly harmonised with the **IFRS** guidance, especially in respect of accounting for derivatives and hedge accounting. However, certain differences remain, especially for entrepreneurs other than financial institutions. The guidance applicable to financial institutions has been substantially harmonised with that applied under **IFRS**.

FINANCIAL ASSETS (continued)**Definition**

IFRS and **Czech GAAP** define a financial asset in a similar way to include: cash; a contractual right to receive cash or another financial asset from another entity or a contractual right to exchange financial instruments with another entity under conditions that are potentially favourable; and equity securities (equity instruments) of another entity. Financial assets include derivatives with positive fair value. Accounting for derivatives is dealt with on page 68. However, **Czech GAAP** excludes from financial assets accrued income and, in a number of specific provisions, trade and other receivables.

Recognition and initial measurement

IFRS **IFRS** requires that an entity recognise a financial asset only when the entity becomes a party to the contractual provisions of a financial instrument. A financial asset is recognised initially at its fair value (which is normally the transaction price), plus, in the case of a financial asset that is not measured at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of that asset.

Czech GAAP Under **Czech GAAP**, upon initial recognition financial assets are measured at cost, including transaction costs, which in most cases results in the same treatment as under **IFRS**.

Classification and subsequent measurement

IFRS define four financial asset categories, whereas **Czech GAAP** defines four categories for the securities recognized in the assets. The classification criteria and requirements for subsequent measurement are presented in the table below.

Under **Czech GAAP**, somewhat different rules apply for financial institutions on one hand (closer to **IFRS**) and entrepreneurs on the other (with more departures from the **IFRS** treatment).

Classification	IFRS	Czech GAAP
Financial assets at fair value through profit or loss		
This category has two sub-categories: financial assets held for trading (described in the next subcategory), and those designated to the category at inception. Any financial asset may, on initial recognition, be classified as fair value through profit or loss.	An irrevocable decision to classify a financial asset as fair value through profit or loss, provided it results in more relevant information because either: <ul style="list-style-type: none"> a) it eliminates or significantly reduces a measurement or recognition inconsistency; b) a group of financial assets, financial liabilities or both is managed and performance is evaluated on a fair value basis; or c) the contract contains one or more substantive embedded derivatives. 	The limitations for the fair value option, i. e. classification of a security in this subcategory are different under Czech GAAP : any security can be designated at fair value through profit or loss at inception except for participation interests that are not publicly traded and the fair value of which cannot be reliably measured.

FINANCIAL ASSETS (continued)

Classification and subsequent measurement (continued)

Classification	IFRS	Czech GAAP
Held-for-trading financial assets		
This subcategory includes debt and equity securities held for sale in the short term. Mandatory inclusion of derivatives.	<p>The positive intent must be to hold the financial asset for a relatively short period, or as part of a portfolio for the purpose of short-term profit-taking.</p> <p>Subsequent measurement at fair value. Unrealised and realised gains and losses recognised in the profit or loss.</p>	Comparable to IFRS.
Held-to-maturity investments		
Financial assets held with a positive intent and ability to hold to maturity. Includes assets with fixed and determinable payments and maturities. Does not include equity securities because they have an indefinite life.	<p>Entity must have the "positive intent and ability" to hold a financial asset to maturity, not simply a present intention.</p> <p>When an entity sells more than an insignificant amount of assets, classified as held-to-maturity, it is prohibited from using the held-to-maturity classification for two full annual reporting periods (known as tainting). The entity must also reclassify all its held-to-maturity assets as available-for-sale assets.</p> <p>Measured at amortised (accrued) cost using the effective yield method.</p>	<p>Comparable to IFRS.</p> <p>Comparable to IFRS.</p> <p>Comparable to IFRS. The effective yield method only required for financial institutions. In insurance companies measured at fair value. Changes in fair value are recognised net of tax effects in equity and recycled to profit or loss when sold, impaired or collected.</p>
Loans and receivables		
Financial assets created by providing money, goods and services directly to the borrower e.g. bonds, customer loans and trade receivables. However, it must not include marketable financial assets. May include loans and receivables purchased (acquired by assignment), provided their intention is similar.	Measured at amortised cost.	<p>Comparable to IFRS.</p> <p>Measured at amortised cost.</p>
Available-for-sale financial assets		
All debt/equity financial assets not covered by the above categories. Includes equity securities, except those classified as held-for-trading and may also include purchased receivables.	<p>Measured at fair value.</p> <p>Changes in fair value are recognised net of tax effects in equity and recycled to profit or loss when sold, impaired or collected.</p> <p>Foreign exchange gains and losses on debt securities are recognised in profit or loss.</p>	<p>Comparable to IFRS</p> <p>Changes in fair value in the case of insurance companies are recorded in the income statement.</p>

FINANCIAL ASSETS (continued)**Reclassification of assets between categories**

IFRS Reclassifications between categories are relatively uncommon under **IFRS** and in the case of financial assets are strictly prohibited in the fair value through profit or loss category until IAS 39 amendment was issued in October 2008. This amendment to IAS 39 Financial Instruments: Recognition and Measurement enabled under specific circumstances reclassifications from the Financial assets at fair value through profit or loss category (but not one designated by entity) and Available-for-sale category to other portfolios.

Reclassifications from the held-to-maturity category as a result of a change of intent or ability are treated as sales and the whole category is being “tainted”. The most common reason for a reclassification out of the category, therefore, is when the whole category is tainted and has to be reclassified as available-for-sale for two years (three reporting dates). In such circumstances, the assets are remeasured to fair value, with any difference recognised in equity.

A financial instrument may be reclassified into the category where the tainted held-to-maturity portfolio has been “cleansed”. In this case, the financial asset’s carrying amount (in practice, fair value) at the date of reclassification is recharacterised as acquisition cost. Any unrealised gains and losses already recognised remain in equity until the asset is impaired or derecognised.

Czech GAAP Reclassifications from the held-for-trading category to the held-to-maturity or the available-for-sale categories were also not permitted, but the reclassification rules arising from the amendment of IAS 39 are applied by reference to IAS 39 also for the securities reclassifications under **Czech GAAP** as these changes were adopted in the **Czech GAAP** in December 2008. Reclassifications from the available-for-sale category to the held-to-maturity category are permitted, provided that certain conditions are met. Measurement methods are not explicitly prescribed, in practice the treatment in accordance with **IFRS** is used.

Impairment

IFRS Entities have to consider impairment when there is an indicator of impairment, such as: the deterioration in the creditworthiness of a counterparty; an actual breach of contract; a high probability of bankruptcy; or the disappearance of an active market for an asset or in the case of an investment in an equity instrument, whether there has been a significant or prolonged decline in the fair value of that investment below its cost. A decline in the fair value of a financial asset below its cost that results from the increase in the risk-free interest rate is not necessarily evidence of impairment. An impairment of a security does not establish a new cost basis.

IFRS requires that, for financial assets carried at amortised cost, the impairment loss is the difference between the asset’s carrying amount and its estimated recoverable amount (defined as present value of expected future cash flows discounted at the instrument’s original effective interest rate). For financial assets carried at fair value, the recoverable amount is usually based on quoted market prices, or if unavailable, the present value of the expected future cash flows discounted at the current market rate. If a loss has been deferred in equity, it must be reclassified to profit or loss.

IFRS requires that changes in the fair value of available-for-sale debt securities, identified as reversals of previously recognised impairment, be recognised in profit or loss. **IFRS** prohibits reversals of impairment on available-for-sale equity securities through profit or loss.

FINANCIAL ASSETS (continued)

Impairment (continued)

Czech GAAP No specific guidance exists on the measurement of impairment of financial assets carried at amortised cost. Only general requirements to reflect the impairment of assets apply. Regulated funds are obliged to reflect impairment, originally recognised in equity, through the income statement in the full extent of the difference between acquisition cost and lower fair value. Banks are subject to special regulations that allow them to fully adopt the **IFRS** impairment rules into their **Czech GAAP** accounting records.

Derecognition of financial assets

Under **IFRS**, an entity recognises the assets that it controls in its statement of financial position, whereas assets that are not subject to the entity's control are derecognised. **Czech GAAP** currently does not contain any specific provision addressing this matter, except for financial institutions, for which the derecognition test is based on the control test, rather than on the assessment of risks and rewards.

IFRS

A financial asset (or part thereof) is derecognised when:

- the rights to the asset's cash flows expire,
- the rights to the asset's cash flows and substantially all risks and rewards of ownership are transferred,
- an obligation to transfer the asset's cash flows is considered to be the case where substantially all risks and rewards are transferred and the following conditions are met:
 - no obligation to pay cash flows unless it collects equivalent cash flows from the transferred asset
 - prohibition from selling or pledging the asset,
 - obligation to remit (return) cash flows without material delay, or
- substantially all the risks and rewards are neither transferred nor retained but control of the asset is transferred.

An entity consolidates any subsidiaries including SPEs before applying the derecognition tests to the consolidated entity. If an entity transfers substantially all the risks and rewards of ownership of the asset (e.g., an unconditional sale of a financial asset), the entity derecognises the asset. If an entity retains substantially all the risks and rewards of ownership of the asset, the entity continues to recognise the asset (the transaction is accounted for as a collateralised borrowing). If an entity neither transfers nor retains substantially all the risks and rewards of ownership of the asset, the entity has to determine whether it has retained control of the asset. Control is based on the transferee's practical ability to sell the asset. If the entity has lost control, the asset is derecognised. If the entity has retained control, it continues to recognise the asset to the extent of its continuing involvement.

If the asset is derecognised on sale to a special purpose entity (SPE), there may nevertheless be a requirement to consolidate that SPE.

On derecognition, the difference between the amount received and the carrying amount of the asset is recognised in profit or loss. Any fair value adjustments on the assets formerly reported in equity are recycled to profit or loss. Any new assets or liabilities arising from the transaction are recognised at fair value.

FINANCIAL ASSETS (continued)**Derecognition of financial assets (continued)**

Czech GAAP **Czech GAAP** currently contains no specific standard addressing this matter. Accounting treatment generally follows the legal form and the legal transfer of ownership. No guidance for repo and reverse repo operations is available. However, a number of entities apply the treatment applicable to financial institutions, which is comparable to **IFRS**. For the most part, when accounting for sales (disposals) and acquisitions of securities, the date of settlement is used. For financial institutions the treatment comparable to **IFRS** is prescribed, which is, however, based on the control test, rather than on the assessment of risks and rewards. Accounting for repo and reverse repo operations is consistent with **IFRS** for financial institutions.

REFERENCES: IFRS: IAS 32, IAS 39, SIC-12. **Czech GAAP:** Decree 500/2002 Coll., Decree 501/2002 Coll.

LIABILITIES

PROVISIONS

IFRS has a specific standard on accounting for provisions. **IFRS** prohibits recognition of provisions for future costs, including costs associated with compliance with proposed but not yet effective legislation. Under **Czech GAAP** in practice a similar treatment is used, but accounting policies for entrepreneurs for the time being allow broader interpretation due to its general requirement for the creation of provisions against risks and losses on business activities, including provisions for the repair and maintenance of tangible fixed assets.

Recognition

IFRS

Requires and allows recognition of a provision only when:

- the entity has a present obligation to transfer economic benefits (legal or constructive) as a result of past events (events prior to the reporting date); and
- it is probable that the entity's assets will be required to settle the obligation; and
- a reliable estimate of the amount of the obligation can be made.

A present obligation arises from an obligating event and may take the form of either a legal obligation or a constructive obligation. An obligating event leaves the entity no realistic alternative other than to settle the obligation created by the event. If the entity can avoid the future expenditure by its future actions, it has no present obligation and a provision is not recognised.

Czech GAAP

Broadly comparable to **IFRS**, but not explicitly defined. Accounting policies for entrepreneurs only stipulate a general requirement to create provisions against risks and losses on business activities and for restructuring. The only exceptions are "legal provisions", which are set aside, for example, for future expenditures for the repairs of tangible fixed assets. Creation and usage of these provisions are regulated by the Act on Tax Deductible Provisions and their creation is not limited by any general accounting definition of a provision (creation of these provisions is a tax-deductible expense, however, a corresponding cash amount must be set aside in a blocked bank account to "cover" such tax deductible provisions). Similar provisions are not permitted under **IFRS**.

Measurement

IFRS

The amount recognised as a provision must be the best estimate of the minimum expenditure required to settle the present obligation as at the reporting date. The entity must discount the anticipated cash flows using a pre-tax discount rate that reflects the current market assessment of the time value of money and those risks specific to the liability, if the effect is material. If a range of estimates is predicted and no amount in the range is more likely than any other amount in the range, the "mid-point" of the range must be used to measure the liability.

Czech GAAP

Financial institutions must discount provisions if the effect is material. This issue is not addressed for entrepreneurs, therefore some reporting entities present their provisions undiscounted.

Restructuring provisions

IFRS

In the case of restructuring, a present obligation exists only when the entity is "demonstrably committed" to the restructuring. An entity is usually demonstrably committed when there is a binding sale agreement (legal obligation), or when the entity has a detailed formal plan for the restructuring and is unable to withdraw because it has started to implement the plan or announced its main features to those affected (constructive obligation). However, if there will be a delay before the restructuring begins, or the restructuring will take an unreasonably long time to complete, then a provision is unlikely to be justified.

PROVISIONS (continued)**Restructuring provisions (continued)**

Czech GAAP Based on the formal restructuring plan approved by the body competent to do so under a special regulation, or by the entity's partners, the entity may create a restructuring provision. The restructuring means a plan whereby the entity's business or the manner of its performance is substantially changed. The restructuring may involve especially the relocation of business activities into another region, plant closures or scaling down or discontinuing a part of business activities. A restructuring provision may be created and used only for direct costs necessarily required for the implementation of the restructuring plan unrelated to the continuing activities of the entity.

Onerous contracts

IFRS Prohibits provisions for future operating losses. However, if an entity is party to a contract that is onerous (the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under the contract), the present obligation under the contract must be recognised and measured as a provision. One of the most common examples relates to leasehold property that has been left vacant.

Czech GAAP No specific guidance is given on onerous contracts, general requirements for the creation of provisions against anticipated risks and losses apply.

REFERENCES: IFRS: IAS 37. **Czech GAAP:** Act on Accounting, Czech accounting standard 004.

Decommissioning, restoration and similar liabilities (asset retirement obligations)

IFRS A liability for the present value of the costs of dismantling, removing or restoring as a result of a legal or constructive obligation is recognised and the corresponding cost included as part of the related property, plant or equipment (PPE). An entity incurs this obligation as a consequence of installing the item or using the item during a particular period for purposes other than to produce inventories during that period.

Changes in the measurement of the liability relating to changes in the estimate of the timing or amount of the future cash flows or changes in the discount rate are recognised immediately with a corresponding adjustment to the carrying amount of PPE. If the PPE asset is measured using the cost model, a decrease in the liability is deducted from the carrying amount of the asset until the full carrying amount of the asset is reduced to zero. The discount rate applied is adjusted as at each reporting date. Changes in the measurement of the liability due to the passage of time (accretion of the discount) are included in profit or loss.

Czech GAAP No specific guidance is available. In practice, there is diversity in accounting for asset retirement obligations. The carrying amount of tangible fixed assets cannot be increased as a result of the creation or change in asset retirement obligations.

REFERENCES: IFRS: IAS 16, IAS 37, IFRIC 1. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll., Czech accounting standard 004.

PROVISIONS (continued)**Liability arising from participation in a specific market – waste electrical and electronic equipment**

IFRS A producer recognises a liability for the cost of waste management for household equipment sold to private households before 13 August 2005 ('historical waste') when it participates in the market during the measurement period. The same principle can be applied to new waste (sold to private households on or after 13 August 2005) if the national legislation treats the new waste in a similar manner as historical waste and the entity is not obligated for costs incurred after it exits the market. Commercial-user entities can also apply the same treatment if the fact pattern is similar to historical waste from private households.

Czech GAAP No specific guidance is available; however, general principles for the creation of provisions should lead to the creation of a provision in such circumstances. Measurement of the provision could vary in practice.

REFERENCES: IFRS: IAS 37, IFRIC 6. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll., Czech accounting standard 004.

CONTINGENCIES**Contingent asset**

IFRS This is a possible asset that arises from past events, and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events, not wholly within the entity's control. When the realisation of the associated benefit, such as an insurance recovery, is virtually certain, the item is recognised as an asset.

Czech GAAP Detailed guidance comparable to **IFRS** does not exist; in practice the treatment is similar to **IFRS**, while anticipated insurance recovery is usually accounted for at the level of the recorded damage with regard to the insurance cover or estimates made by the insurance company.

Contingent liability

IFRS This is a possible obligation whose outcome will be confirmed only on the occurrence or non-occurrence of uncertain future events outside the entity's control. A contingent liability can also be a present obligation that is not recognised because it is not probable that there will be an outflow of economic benefits, or the amount of the outflow cannot be reliably measured. Contingent liabilities are disclosed unless the probability of outflows is remote.

Czech GAAP An entity must disclose material potential losses in the notes for which a provision has not been created and the realisation of which depends on (is contingent on) the occurrence of contingent future events.

REFERENCES: IFRS: IAS 37. **Czech GAAP:** Decree 500/2002 Coll.

DEFERRED TAX

Although both frameworks require full provision for deferred tax on all so-called temporary differences, there are differences in the methodology as set out in the table below. **Czech GAAP** requires accounting for deferred tax in individual financial statements only by entities that undergo mandatory audits and in all consolidated financial statements.

Issue	IFRS	Czech GAAP
General considerations		
General approach	Full provision on all temporary differences, with only a limited number of exceptions (see below).	Comparable to IFRS , however no exceptions stated.
Basis for deferred tax assets and liabilities	Temporary differences, i.e., the difference between carrying amount and tax base of assets and liabilities (see exceptions below).	Comparable to IFRS .
Exceptions (i.e., deferred tax is not provided on the temporary difference)	<p>Goodwill, which is not deductible for tax purposes, does not give rise to a taxable temporary difference.</p> <p>Initial recognition of an asset or liability in a transaction that (i) is not a business combination and (ii) at the time of the transaction, affects neither accounting nor taxable profit.</p> <p>Other amounts that do not have a tax consequence (commonly referred to as permanent differences) exist and depend on the tax rules and jurisdiction of the entity.</p>	<p>For entrepreneurs, no exception (deferred tax is provided on goodwill). In the case of financial institutions comparable to IFRS. In practice some entities do not recognise deferred tax on goodwill, similarly to IFRS – this approach is considered acceptable.</p> <p>No similar exemption.</p>
Specific applications		
Unrealised intra-group profits, e.g., on inventory	Deferred tax recognised at the buyer's tax rate.	Not specified.
Revaluation of PPE and intangible assets	Deferred tax recognised in equity.	Not applicable – revaluation of such assets is not allowed.
Revaluation of financial assets	Deferred tax is recognised in profit or loss unless changes in the carrying amount of available-for-sale assets are taken to equity, in which case deferred tax is taken to equity.	Comparable to IFRS .

DEFERRED TAX (continued)

Issue	IFRS	Czech GAAP
Specific applications (continued)		
Foreign exchange differences on financial statements prepared in a foreign currency on foreign transactions that are part of the operations of the parent company (for instance, a foreign branch)	Deferred tax is recognised on the difference between the carrying amount determined using the historical rate of exchange and the tax base determined using the reporting date exchange rate.	No specific guidance.
Investments in subsidiaries, joint ventures and associated companies: treatment of undistributed profit	Deferred tax is recognised except when the parent (reporting entity) is able to control temporary differences and if it is probable that the temporary difference will not be reversed in the foreseeable future.	No specific guidance, no exceptions exist.
Measurement of deferred tax		
Tax rates	Tax rates and tax laws that have been enacted or substantively enacted for the period of anticipated realisation of temporary differences apply.	Tax rates and tax laws that have been enacted for the period of anticipated realisation of temporary differences.
Recognition of deferred tax asset	Deferred tax assets must be recognised if it is probable that sufficient taxable profit will be available against which the temporary difference can be utilised.	Comparable to IFRS .
Discounting	Prohibited.	Prohibited.
Business combinations – acquisitions		
Step-up of acquired assets/liabilities to fair value	Deferred tax is provided unless the tax base of assets is also stepped up.	Comparable to IFRS .
Previously unrecognised tax losses of the acquirer	Deferred tax asset is recognised if, as a result of the acquisition, the recognition criteria for the deferred tax assets are met.	No specific guidance, but in practice the approach consistent with IFRS is applied.
Tax losses of the acquiree	Similar requirements as for the acquirer except that the offsetting credit is recorded against goodwill.	Comparable to IFRS .
Presentation of deferred tax		
Offset of deferred tax assets and liabilities	Permitted only when the entity has a legally enforceable right to set off, and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.	Comparable to IFRS .
Current/non-current classification	The deferred tax assets and liabilities must only be classified as non-current, with supplemental note disclosure for: 1) the components of the temporary differences, and 2) amounts expected to be recovered within 12 months and more than 12 months of the reporting date.	Comparable to IFRS , no supplemental split of current/non-current is required.
Reconciliation of actual and expected tax expense	Required. Computed by applying the applicable tax rates to accounting profit, also disclosing the basis on which the applicable tax rates are computed.	Not required, often disclosed as a matter of best practise.

REFERENCES: IFRS: IAS 12. Czech GAAP: Decree 500/2002 Coll., Czech accounting standard 003.

GOVERNMENT GRANTS

IFRS Government grants (or contributions) received as compensation for expenses already incurred are recognised once the conditions for their being received have been met and there is reasonable assurance that the grant will be received. Revenue-based grants are deferred in the statement of financial position and released to profit or loss to match the related expenditure that they are intended to compensate. Capital-based grants must be deferred and matched with the depreciation on the asset for which the grant arises or reduce the cost of the subsidised asset.

Grants that relate to recognised assets must be presented in the statement of financial position either as deferred income, or by deducting the grant in arriving at the asset's carrying amount, in which case the grant is recognised in profit or loss as a reduction of depreciation. Specific rules apply for biological assets.

Czech GAAP Grants for the purpose of covering expenses are recorded in income consistently, in terms of time and substance, with the recognition of expenses for which the subsidy was provided. Grants for interest expense not capitalised in the carrying amount of fixed assets are credited to financial income. Grants for the acquisition of fixed assets (including grants for interest expense capitalised) reduce the cost of acquired assets or own costs on internally generated assets. In the case of grants at 100%, assets are recorded off balance sheet. Recording investment grants as deferred income is not permitted. No specific rules apply for biological assets.

Grants – biological assets

IFRS An unconditional government grant related to a biological asset measured at its fair value must be recognised as income, when the grant becomes receivable. If a government grant relating to a biological asset measured at its fair value is conditional, the grant must be recognised when the conditions are met. If a grant relates to a biological asset measured at cost, then the accounting treatment specified for government grants generally is applied.

Czech GAAP Not specified (biological assets are not measured at fair value).

REFERENCES: IFRS: IAS 20, IAS 41. **Czech GAAP:** Decree 500/2002 Coll., Czech accounting standard 017.

LEASES – LESSEE ACCOUNTING**Finance leases**

IFRS Requires recognition of an asset held under a finance lease (see classification criteria on page 49) with a corresponding obligation to pay future rentals, at an amount equal to the lower of the fair value of the asset and the present value of the minimum lease payments (MLPs) at the inception of the lease. The asset is normally depreciated over its useful life. However, using the shorter lease term and useful life is required if there is no reasonable certainty of the lessee obtaining ownership of the asset. The interest rate implicit in the lease must normally be used to calculate the present value of the MLPs. The lessee's incremental borrowing rate may be used, if the implicit rate is unknown.

Czech GAAP The lessee does not capitalise the asset, nor recognise the related liability. Accounting for finance and operating leases is the same. On subsequent acquisition the asset is recognised by the lessee at the residual value determined in the lease agreement at the inception of the lease.

LEASES - LESSEE ACCOUNTING (continued)**Operating leases**

Under both **IFRS** and **Czech GAAP**, the rental expense under an operating lease must generally be recognised on a straight-line basis over the lease term.

Incentives

A lessor often provides lease incentives to encourage the lessee to renew a lease arrangement. Under **IFRS**, the lessee must recognise the aggregate benefit of incentives as a reduction of the rental expense over the lease term. The incentive must be amortised on a straight-line basis unless another systematic basis is more representative of the pattern of the lessee's benefit from the use of the leased asset.

No specific guidance is given on this matter is given under **Czech GAAP**.

SALE AND LEASEBACK TRANSACTIONS

In a sale and leaseback transaction, the seller-lessee sells an asset to the buyer-lessor and leases the asset back. There are certain differences in the rules on dealing with profits and losses arising on sale and leaseback transactions across both frameworks. These are highlighted in the table below:

Issue	IFRS	Czech GAAP
Finance lease		
Profit or loss on sale	Deferred and amortised over the lease term.	No guidance is given on this matter. Czech GAAP does not define specific rules for finance leases and the accounting treatment follows the legal form.
Operating lease		
Sale at fair value	Immediate recognition.	No specific guidance.
Sale at less than fair value	Immediate recognition unless the difference is compensated by lower future rentals, then defer the difference over the period over which the asset is expected to be used.	No specific guidance.
Sale at more than fair value	The difference (profit) is deferred and amortised over the period for which the asset is expected to be used.	No specific guidance.

REFERENCES: IFRS: IAS 17, SIC-15. **Czech GAAP:** Decree 500/2002 Coll.

FINANCIAL LIABILITIES**Definition**

IFRS defines a financial liability as a contractual obligation to deliver cash or a financial asset to another entity, or to exchange financial instruments with another entity under conditions that are potentially unfavourable. Financial liabilities include derivatives with negative fair value (under **IFRS**, these include many contracts that will or may be settled in the entity's own equity instruments). Derivatives are dealt with on page 68.

FINANCIAL LIABILITIES (continued)**Classification**

IFRS Where there is a contractual obligation (or economic compulsion) of the issuer of an instrument to deliver either cash or another financial asset to the holder, that instrument meets the definition of a financial liability, regardless of the manner in which the contractual obligation will be settled.

Preferred shares that are not redeemable, or that are redeemable solely at the option of the issuer, and where distributions are at the discretion of the issuer, are classified as equity. However, preferred shares requiring the issuer to redeem for a fixed or determinable amount at a fixed or determinable future date, or where the holder has the option of redemption, are classified as liabilities.

Where the settlement of a financial instrument such as a preferred share is contingent on uncertain future events beyond the control of both the issuer and the holder, the issuer must classify the financial instrument as a liability. However, an instrument that is settled by an entity's own equity shares is classified as a liability if the number of shares varies in such a way that the fair value of the shares issued equals the obligation.

Puttable instruments (financial instruments that give the holder the right to put the instrument back to the issuer for cash or another asset) are liabilities.

Split accounting is applied to convertible debt – see below.

Czech GAAP No specific detailed guidance corresponding to **IFRS** is available. Units of open-ended mutual funds, which are by law puttable instruments, are classified as equity.

Convertible debt

IFRS “Split accounting” is used whereby the proceeds of issuing debt are allocated between the two components: the equity conversion rights (recognised in equity); and the liability, recognised at fair value calculated by discounting at a market rate for a non-convertible debt (recognised in liabilities).

Czech GAAP No explicit requirement for “split accounting”. Compound financial instruments are rarely used in practice.

Measurement

IFRS There are only two categories of financial liabilities: those measured at fair value through profit or loss (includes trading liabilities) and all others. Initial measurement of liabilities at fair value through profit or loss is at fair value, while for all other financial liabilities it is fair value less direct transaction costs. All derivatives that are liabilities (except qualifying hedging instruments) are trading liabilities. Other trading liabilities always include a short position from securities. After initial recognition, financial liabilities at fair value through profit or loss are measured at fair value (the changes in fair value are recognised in profit or loss for the period). All other financial liabilities are carried at amortised cost.

Czech GAAP The accounting of financial institutions is similar to **IFRS**. The accounting of entrepreneurs is not specifically defined, except for derivatives, which are always measured at fair value through profit and loss. Short positions in securities are usually fair valued. Non-interest bearing financial liabilities are not discounted under **Czech GAAP**.

FINANCIAL LIABILITIES (continued)**Derecognition of financial liabilities**

- IFRS** A financial liability must be derecognised when: the obligation specified in the contract is discharged; cancelled or expires; or the primary responsibility for the liability is legally transferred to another party. The difference between the carrying amount of a liability (or a portion thereof) extinguished or transferred and the amount paid for it must be recognised net in profit or loss for the period.
- Czech GAAP** Specific guidance for financial institutions only – comparable to **IFRS**. Entrepreneurs follow the legal form of the contractual arrangement.

REFERENCES: IFRS: IAS 32, IAS 39. **Czech GAAP:** Czech accounting standard 101.

EQUITY INSTRUMENTS**Recognition and classification**

- IFRS** An instrument is classified as equity when it does not contain an obligation to transfer economic resources. Preference shares, which are not redeemable, or redeemable solely at the option of the issuer, and where distributions are at the issuer's discretion, are classified as equity. Only derivative contracts that result in the delivery of a fixed amount of cash, or other financial asset for a fixed number of an entity's own equity instruments, are classified as equity instruments. All other derivatives on own equity are treated as derivatives.
- Czech GAAP** Equity is split between share capital (registered capital), capital contributions and other equity categories. There is no "mezzanine" category. Preference shares with liability elements in practice do not exist. The legal form is decisive; puttable units of open-ended mutual funds are therefore treated as equity.

Purchase of own shares

- IFRS** When an entity's own shares are repurchased, the shares are shown as a deduction from shareholders' equity. Any profit or loss on the subsequent sale of the shares is shown as a change in equity.
- Czech GAAP** For financial institutions comparable to **IFRS**. For entrepreneurs, own shares are also shown as a deduction from shareholders' equity; however, the performance treatment is not explicitly stipulated in the guidance and, in practice, joint stock companies report the profit or loss on the sale of own shares in the income statement following the general share derecognition rules. The acquisition of own shares is recorded as at the date of arranging an acquisition deal.

Dividends on ordinary shares

- IFRS and Czech GAAP** Presented as a deduction in the statement of changes in shareholders' equity in the period when authorised by shareholders.

REFERENCES: IFRS: IAS 32, IAS 39, SIC-16. **Czech GAAP:** Czech accounting standards 012 and 108.

DERIVATIVES

IFRS and **Czech GAAP** both specify rules for the recognition and measurement of derivatives.

Definition

IFRS defines a derivative as a financial instrument whose value changes in response to a specified variable or underlying rate, requires little or no net investment and is settled at a future date.

The definition under **Czech GAAP** is comparable to **IFRS**.

Initial measurement

Under **IFRS** and **Czech GAAP**, all derivatives are recognised in the statement of financial position as either financial assets or financial liabilities. Under **IFRS**, they are initially measured at fair value, whereas under **Czech GAAP** they are initially measured at cost. Under **IFRS**, the direct external transaction costs are excluded, whereas in **Czech GAAP** direct external transaction costs are included.

Subsequent measurement

IFRS and **Czech GAAP** require subsequent measurement of all derivatives at their fair value, regardless of any hedge relationship that might exist. Changes in a derivative's value are recognised in profit or loss as they arise, unless they satisfy the criteria for cash flow hedge accounting outlined below. Under **IFRS** and **Czech GAAP**, a derivative whose fair value cannot be measured reliably is carried at cost less impairment or amortisation until settlement.

Embedded derivatives

Under **IFRS**, derivatives embedded in a host contract have to be separated from that contract, unless the whole instrument is measured at fair value or the economic characteristics and risks of the embedded derivative are the same as those of the host contract. Under **Czech GAAP** entrepreneurs have the option not to separate the derivative from the host contract or follow guidance similar to **IFRS**. Financial institutions have to follow guidance close to **IFRS** except for non-financial instrument contracts denominated in an other than functional currency, which are not considered embedded derivatives.

Under both **IFRS** and **Czech GAAP** fair value excludes transaction costs.

HEDGE ACCOUNTING

Under **IFRS** and **Czech GAAP**, detailed guidance is set out in the respective standards dealing with hedge accounting.

Criteria for hedge accounting

Under both **IFRS** and **Czech GAAP**, hedge accounting is permitted (not required) provided that an entity meets specific qualifying criteria in relation to documentation and hedge effectiveness. Both frameworks require documentation of the entity's risk management objectives and strategies and how the effectiveness of the hedge will be assessed. Hedge instruments must be highly effective in offsetting the exposure of the hedged item to changes in the fair value or cash flows, and the effectiveness of the hedge must be measured reliably on a continuous basis.

IFRS does not require 100% effectiveness of a hedge to allow the use of hedge accounting. Under **IFRS**, a hedge qualifies for hedge accounting if the expectation is that changes in fair values or cash flows of the hedged item are almost fully offset (i.e., nearly 100%) by the changes in the fair value or cash flows of the hedging instrument ("prospective" test) and "actual" results are within a range of 80% to 125% ("retrospective" test). The **Czech GAAP** rules basically correspond to **IFRS**. However, for the "prospective" test under **Czech GAAP**, a range of 80% to 125% is also used.

HEDGE ACCOUNTING (continued)**Hedged items**

In addition to the general criteria for hedge accounting, **IFRS** outlines rules for the designation of specific financial assets and liabilities as hedged items. These are outlined below.

- Held-to-maturity investments cannot be designated as a hedged item with respect to interest-rate risk, because changes in interest rates are not recognised for held-to-maturity investments.
- If the hedged item is a financial asset or liability, it may be designated as a hedged item only in relation to those risks where the effectiveness can be measured.
- If the hedged item is a non-financial asset or liability, it may be designated as a hedged item only for foreign currency risk, or for all risks entirely because of the difficulty of isolating other risks.
- If similar assets or similar liabilities are aggregated and hedged together as a group, the change in fair value attributable to the hedged risk for individual items must be proportionate to the change in fair value of the group.

Under **Czech GAAP**, a detailed explanation is available in the Czech accounting standards which is comparable to **IFRS**. Hedged items (instruments) may be assets or liabilities (or their parts), legally enforceable contracts that are not recognised on a balance sheet, and anticipated future transactions that are not covered by contracts and the realisation of which is highly probable. Assets and liabilities with similar characteristics, which are subject to hedging of the same risk type and category, may be aggregated and hedged as a group.

Hedging instruments

In most cases only a derivative instrument can qualify as a hedging instrument. However, **IFRS** and **Czech GAAP** permit a non-derivative (such as a foreign currency borrowing) to be used as a hedging instrument for foreign currency risk.

Under **IFRS** a written option cannot be designated as a hedging instrument unless it effectively secures a purchase option. A similar interpretation is used in practice under **Czech GAAP** as the option writer has no control over the exercise of the option.

Hedge relationships

Exposure to risk can arise from: changes in the fair value of an existing asset or liability; changes in the future cash flows arising from an existing asset or liability; or changes in future cash flows arising from a transaction that is not yet recognised.

IFRS Recognises several types of hedge relationships: a fair value hedge where the risk being hedged is a change in the fair value of a recognised asset or liability; a cash flow hedge where the risk being hedged is the potential volatility in future cash flows; a hedge of a net investment in a foreign entity, where the hedging instrument is used to hedge the currency risk of a net investment in a foreign entity. A forecasted transaction must be highly probable to qualify as a hedged item.

Czech GAAP Comparable to **IFRS**.

HEDGE ACCOUNTING (continued)

Fair value hedges

IFRS Hedging instruments are measured at fair value. The hedged item is adjusted for changes in its fair value, but only due to the risks being hedged over the duration (term) of the hedge relation. Gains and losses on fair value hedges, for both the hedging instrument and the item being hedged, are recognised in profit or loss.

Czech GAAP Comparable to **IFRS**.

Cash flow hedges

IFRS Hedging instruments are measured at fair value, with gains and losses on the hedging instrument, where they are effective, initially deferred in equity and subsequently released to profit or loss concurrent with the earnings recognition pattern of the hedged item. Gains and losses on financial instruments used to hedge forecasted non-financial asset or liability acquisitions may be included in the cost of the non-financial asset or liability – so-called “basis adjustment” – but this is not permitted for financial assets or liabilities. In the case of financial assets or liabilities, the equity balance is gradually transferred to profit or loss against the earnings effects of the hedged item.

Czech GAAP Comparable to **IFRS**, except for financial assets and liabilities where the basis adjustment is used as well.

Hedging of net investments in foreign operations

IFRS Similar treatment to cash flow hedges; the hedging instrument is measured at fair value with gains/losses deferred in equity, to the extent that the hedge is effective, together with exchange differences arising on the entity’s investment in the foreign operation. These gains/losses are transferred to profit or loss on disposal of the foreign operation. **IFRS** allows the full gains and losses on hedges of a net investment in a foreign operation to be deferred in equity (including any hedge ineffectiveness), provided the hedging instrument is a non-derivative (e.g. a borrowing).

Czech GAAP Comparable to **IFRS**.

Disclosure

The extensive disclosure requirements in **IFRS** apply to all entities. The disclosures include general information about the entity’s use of financial instruments, fair value information, details of hedging activities and liquidity information.

In **Czech GAAP**, the requirements for disclosure of information on derivatives are not, in comparison with **IFRS**, so specific. More detailed and more extensive disclosures are required from financial institutions.

IFRS requires further disclosures on fair values, including the extent to which fair values are determined by reference to published price quotations, or are estimated using valuation techniques. If a fair value is estimated using a valuation technique and this is sensitive to valuation assumptions that are not supported by observable market prices, a statement of this fact and the effect on the fair value of using a range of reasonably possible alternative assumptions shall be disclosed.

REFERENCES: IFRS: IAS 32, 39. **Czech GAAP:** Decree 500/2002 Coll., 501/2002 Coll., Czech accounting standards.

EARNINGS PER SHARE

Under **IFRS**, earnings per share (EPS) must be disclosed for listed entities and entities that are in the process of listing (quoting) their shares. **Czech GAAP** does not require disclosure of earnings per share in the financial statements, except for investment funds and mutual funds which recognise the basic earnings per share in the notes. However, Czech-listed entities are required to apply **IFRS** for their consolidated and separate financial statements.

Basic EPS

IFRS Basic EPS is calculated as profit available to common shareholders, divided by the weighted average number of shares in issue during the period. Shares issued as a result of a bonus issue (the issue covered by the issuer's equity) are treated as if in issue for the whole year. Bonus issues occurring after the year-end must be incorporated into the calculations. For rights issues, a theoretical ex-rights formula is used. Comparative EPS for past periods is adjusted for bonus issues and rights issues.

Diluted EPS – basis

IFRS There is no “de minimis” dilution threshold below which diluted EPS need not be disclosed. For diluted EPS, earnings are adjusted for the after-tax amount of dividends and interest is recognised in the period in respect of the dilutive potential ordinary shares and for any other changes in profit or loss that would result from the conversion of the dilutive potential ordinary shares. The conversion is deemed to have occurred at the beginning of the period or, if later, the date of the issue of potential dilutive ordinary shares.

Diluted EPS – share option

IFRS The “treasury stock” method is used to determine the effect of share options and warrants. The assumed proceeds from the issue of the dilutive potential ordinary shares are considered to have been used to repurchase shares at fair value. The difference between the number of shares issued and the number of shares that would have been issued at fair value is treated as an issue of ordinary shares for no consideration (i.e., a bonus issue) and is factored into the denominator used to calculate the diluted EPS. The earnings figure is not adjusted for the effect of share options/warrants.

Czech GAAP No guidance is given on the subject of diluted EPS, bonus issues and rights issues, however, listed entities follow **IFRS**.

REFERENCES: IFRS: IAS 33. **Czech GAAP:** Decree 501/2002 Coll.

DISCLOSURE OF RISKS ARISING FROM FINANCIAL INSTRUMENTS

IFRS The entity shall disclose information enabling those who make use of financial statements to evaluate the nature and extent of risks arising from financial instruments to which the entity is exposed. Extensive disclosures ‘through the eyes of management’ of the reporting entity are required.

Czech GAAP An entity using investment or similar instruments shall disclose information enabling those who make use of financial statements to evaluate the financial position and performance

- (i) on goals and methods of risk management, including policies used to hedge transactions by hedging derivatives,
- (ii) on price, credit and liquidity risk exposures.

REFERENCES: IFRS: IFRS 7. **Czech GAAP:** Act on Accounting, Article 21h.

RELATED PARTY TRANSACTIONS

The objective of the disclosures required by **IFRS** in respect of related party relationships and transactions is to ensure that those who make use of financial statements are made aware of the extent to which those statements might be influenced by the existence of related parties.

Under **IFRS**, related party relationships are generally determined by reference to the control or indirect control of one party over another or by the existence of joint control or significant influence of one party over another.

Under **Czech GAAP**, the definition of related party refers to **IFRS**.

If the relationship is one based on control, certain disclosures are always required under **IFRS** (regardless of whether transactions between the parties have taken place); these include the existence of the related party relationship, the name of the related party and the name of the ultimate controlling party.

Disclosures and exemptions

IFRS There is no specific requirement in **IFRS** to disclose the name of the related party (other than the ultimate controlling party, parent entity and, in the separate financial statements, subsidiaries) or the amounts involved in individual transactions. There is a requirement to disclose balances for each major category of related parties. However, the above-mentioned disclosures would appear to be needed in specific cases in order to meaningfully present the “elements” of the transaction.

IFRS also requires disclosure of the compensation of key management personnel in total and by category of compensation.

Exemptions from disclosures about related party transactions in the financial statements of subsidiaries are limited: the subsidiary must be wholly owned and the parent must have its registered office in the same country and prepare consolidated financial statements.

State-controlled entities are required to disclose related party transactions under **IFRS**.

Czech GAAP Disclosure requirements are quite similar to **IFRS**. The definition of related parties is taken directly from **IFRS** by reference. Entities have to disclose at least those transactions that have a material impact on the financial statements and have not been concluded under standard commercial terms.

REFERENCES: IFRS: IAS 24. **Czech GAAP:** Decree 500/2002 Coll., 501/2002 Coll.

SEGMENT REPORTING

IFRS has specific requirements for the identification, measurement and disclosure of segment information. Similarities and differences are reflected in the following table. **Czech GAAP** only requires reporting of the revenue split from ordinary activities (divided by type of ordinary activity and split between domestic and export sales), though the definition of a “segment” is not available in **Czech GAAP**. Financial institutions are required to split assets by individual main segments and geographical sectors, but without giving a more detailed definition of these terms. The guidance in **Czech GAAP** for financial institutions was derived from IAS 14, which was superseded by the new standard **IFRS 8**. Czech-listed companies have to use **IFRS**, therefore the scope difference relates to non-listed public interest entities only.

SEGMENT REPORTING (continued)

Issue	IFRS
General requirements	
Scope	Public entities and entities in the process of filing. Non-public entities may choose full compliance.
Format	Based on operating segments and on how the chief operating decision-maker evaluates financial information for the purposes of allocating resources and assessing performance.
Identification of segment	
General approach	Based on the internally reported operating segments.
Aggregation of similar operating segments	Specific aggregation criteria are given to determine whether two or more operating segments are similar.
Threshold for reportable segments	Revenue, result or assets are 10% or more of all segments. If revenues of reported segments are below 75% of the total, additional segments are reported until the 75% threshold is reached.
Measurement	
Accounting policies for segments	Those adopted for internal reporting to the chief operating decision-maker for the purposes of allocating resources and assessing performance.
Main disclosures	
Factors used to identify reportable segments	Disclosure required includes basis of organisation (for example, based on products and services, geographical areas, regulatory environments) and types of product and service from which each segment derives its revenues.
Profit and assets for each reportable segment	Required.
Components of profit of each reportable segment	Required if included in the measure of segment profit or loss reviewed by the chief operating decision-maker, or are otherwise regularly provided to the chief operating decision-maker, even if not included in that measure of segment profit or loss: <ul style="list-style-type: none"> - third-party revenues; - inter-segment revenues; - interest income; - interest expense; - depreciation and amortisation; - other material items disclosed in accordance with IAS 1; - share of results from equity accounting; - income tax expense; - material non-cash items other than depreciation and amortisation.
Liabilities of reportable segment	Required if regularly reported to chief operating decision-maker.
Other items to be disclosed by reportable segment	Investments accounted for by equity method and additions to certain non-current assets (principally PPE and intangible assets) where included in the assets reported to the chief operating decision-maker or are otherwise regularly reported to the chief operating decision-maker.
Major customers	Total revenue is disclosed, as well as the relevant segment that reported the revenues, for each external customer greater than or equal to 10% of consolidated revenue.
Geographical information	Third-party revenues and certain non-current assets (principally PPE and intangible assets) located in the country of domicile and all foreign countries (in total and, if material, by country) are disclosed.
Third-party revenues	Also disclosed for each product and service if this has not already been disclosed.
Reconciliations of a segment to the corresponding totals of the entity	Reconciliations of total segment revenue, total segment measures of profit or loss, total segment assets, total segment liabilities and any other significant segment totals is required.

REFERENCES: IFRS: IFRS 8. Czech GAAP: Decree 500/2002 Coll.

DISCONTINUED OPERATIONS

Czech GAAP does not specifically define discontinued operations.

Issue	IFRS
Definition	A component of an entity (operations and cash flows that can be clearly distinguished operationally and for financial reporting) that has either been disposed of or is classified as held-for-sale and represents a separate major line of business or geographical area of operations, or is a subsidiary acquired exclusively with a view to resale.
Envisaged timescale	Completed within a year, with limited exceptions.
Starting date for disclosure	From the date on which a component has been disposed of or, if earlier, is classified as held-for-sale.
Measurement	Lower of the carrying value or fair value less costs to sell.
Presentation	A single amount is presented on the face of the statement of comprehensive income comprising the post-tax profit or loss of discontinued operations and an analysis of this amount either on the face of the statement of comprehensive income or in the notes for both current and prior periods.
Ending date of disclosure	Until completion of the discontinuance.
Comparatives	Income statement re-presented for effects of discontinued operations but not balance sheet.

Czech GAAP does not provide specific instructions for the measurement of discontinued operations and disclosure thereof. However, if the impact on the financial position of the entity is material, relevant disclosures should be provided in the notes.

REFERENCES: IFRS: IFRS 5.

EVENTS AFTER THE REPORTING DATE**Adjusting events after the reporting date**

IFRS Adjusting events that occur after the reporting date are defined as events that provide additional evidence of conditions that existed as at the reporting date and materially affect the amounts included. The amounts recognised in the financial statements must be adjusted to reflect the adjusting events after the reporting date.

Czech GAAP For the period commencing on the reporting date and ending at the point of time of the completion of the financial statements, entities are obliged to report in the notes disclosure of facts that provide additional evidence of conditions or situations that existed as at the reporting date and of facts that as contingent conditions or situations existed as at the reporting date, the outcome of which materially change the view on the entity's financial position.

Non-adjusting events after the reporting date

IFRS Non-adjusting events after the reporting date are defined as material events that occurred after the reporting date and are indicative of conditions that arose after the reporting date. The nature and estimated financial effects of such events are disclosed to prevent the financial statements from being misleading.

Czech GAAP See above.

EVENTS AFTER THE REPORTING DATE (continued)**The announcement of a dividend relating to the financial year just ended**

IFRS This event is a non-adjusting event.

Czech GAAP The same treatment as under **IFRS**.

REFERENCES: IAS: IAS 10. **Czech GAAP:** Act on Accounting, Decree 500/2002 Coll.

INTERIM FINANCIAL REPORTING**Stock exchange requirements**

IFRS The IASB does not mandate that public entities whose shares are listed produce interim statements, but does encourage interim reporting – see additional guidance below.

Czech GAAP Requires interim reporting in certain specific and rather extraordinary situations. Entities publicly traded on Czech capital markets report under **IFRS**.

Additional guidance (IFRS)

Additional guidance under **IFRS** includes the following:

- consistent and similar basis for preparation of interim financial information with previously reported annual data and from one period to the next;
- use of accounting policies consistent with the previous annual financial statements, together with adoption of any changes to accounting policies that it is known will be made in the year-end financial statements (for example, application of a new standard);
- preparation of the interim statements using a “discrete approach” to revenue and expenditure recognition; that is, viewing the interim period as a distinct accounting period, rather than part of the annual cycle. Hence, incomplete transactions must be treated in the same way as at the year end. For interim results, the tax charge is based on an estimate of the annual effective tax rate applied to the interim results. Impairment losses recognised in interim periods in respect of goodwill, or an investment in either an equity instrument or a financial asset carried at cost, cannot be reversed later on;
- summarised statements of comprehensive income, financial position, changes in equity and cash flows, and selected explanatory notes; and
- a narrative commentary.

Under **IFRS**, comparatives for the statement of the financial position in interim financial information are taken from the last annual financial statements (basically, the opening statement of the financial position of the current period). Under **IFRS**, quarterly interim reports must contain comparatives (other than for the statement of financial position) for the cumulative period to date and the corresponding period of the preceding year to the same date. Under **Czech GAAP**, no additional guidance is given on the disclosure of comparatives in interim financial statements is available and, in practice, information taken from the income statement for the corresponding prior year period is used. The concept of interim financial statements under the Act on Accounting is considerably narrower, since it only includes financial statements, the preparation of which is prescribed by law or other regulations.

REFERENCES: **IFRS:** IAS 34. **Czech GAAP:** Act on Undertaking on Capital Market, Act on Accounting.

Subject	Page	Subject	Page
Accounting estimates, changes in	24	Financial statements: - contents and presentation	18
Accounting policies, changes in	23	First-time adoption of accounting framework	16
Acquisitions	32	Foreign currency translation	30
Associates	27		
		Goodwill	34
Barter transactions	38	Government grants	64
Biological assets	53		
Business combinations	32	Hedge accounting	68
Business combinations – disclosure	36	Historical cost	15
Business combinations – subsequent adjustments	35	Hyperinflation	31
Capitalisation of borrowing costs	51	Impairment	50
Cash equivalents	22	Income statement	20
Common control transactions	36	Intangible assets	44
Components of financial statements	18	Intangible assets – website development costs	44
Comparatives	18	Interest expense	40
Computer software	44	Interim financial reporting	75
Conceptual framework	14	Inventories	52
Consolidation difference	34	Investment property	51
Consolidation of subsidiaries	25		
Construction contracts	38	Joint ventures	28
Contingencies	61		
Contingent consideration	32	Leases – classification	49
Convertible debt	66	Leases – lessee accounting	64
Correction of errors	23	Leases – lessor accounting	65
		Leases – sale and leaseback	65
Debt securities	56		
Deferred tax	62	Minority interests	33
Depreciation	47	Monetary and non-monetary items	30
Derecognition of financial assets/liabilities	56, 67		
Derivatives	68	Negative goodwill	35
Disclosure of risks arising from financial instruments	71		
Discontinued operations	74	Preference shares	66
Dividends	67	Property, plant and equipment	46
		Proportionate consolidation	29
Earnings per share	71	Provisions	59
Employee benefits – compensated absences	43	Purchase method	32
Employee benefits – pensions	40	Purchase of own shares	67
Employee benefits – termination benefits	43		
Employee benefits – share based payments	42	Related party transactions	72
Equity instruments	67	Reporting currency	17
Equity method of accounting	27	Research and development costs	44
Events after the reporting date	74	Restructuring provisions	33, 59
Exceptional items	21	Revenue recognition	37
Expenses	40		
Extraordinary items	21	Segment reporting	72
		Special purpose entities	26
Fair presentation override	15	Statement of cash flows	22
Financial assets	53	Statement of comprehensive income	20
Financial instruments	65	Statement of changes in shareholders' equity	21
Financial liabilities	65	Statement of financial position	19
		Subsidiaries	25

Act on Accounting	Act No. 563/1991 Coll., on Accounting, as amended
Act on Income Taxes	Act No. 586/1992 Coll., on Income Taxes, as amended
Act on Securities	Act No. 591/1992 Coll., on Securities, as amended
Act on Undertaking on Capital Market	Act No. 256/2004 Coll., on Undertaking on Capital Market
Commercial Code	Act No. 513/1991 Coll., the Commercial Code, as amended
Act on Transformations	Act. No. 125/2008 Coll., on Transformation of commercial companies and cooperatives
Czech accounting standards	Czech accounting standards issued by the Ministry of Finance of the Czech Republic
Decree 500/2002 Coll.	Decree No. 500/2002 Coll., implementing certain provisions of Act No. 563/1991 Coll., on Accounting for entities that are entrepreneurs, using the double-entry bookkeeping, as amended by Decree No. 469/2008 Coll.
Decree 501/2002 Coll.	Decree No. 501/2002 Coll., implementing certain provisions of Act No. 563/1991 Coll., on Accounting for entities that are banks and other financial institutions, as amended by Decree No. 470/2008 Coll.
Decree 502/2002 Coll.	Decree No. 502/2002 Coll., implementing certain provisions of Act No. 563/1991 Coll., on Accounting for entities that are insurance companies, as amended by Decree No. 351/2007 Coll.
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IFRIC	International Financial Reporting Interpretation Committee
IFRS	International Financial Reporting Standards
SIC	Standing Interpretation Committee

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