

Amendment to the Act on Accounting from May 2015



Act No. 431/2002 Coll. on Accounting (hereafter referred as the "Act on Accounting" or the "Act") has been amended by Act No. 130/2015 Coll. of 6 May 2015. Certain changes will enter into force on 1 July 2015, others on 1 January 2016, and some will become effective on 1 January 2017.

Most of these changes have been made as a result of the Slovak Republic's obligation to implement Directive No. 2013/34/EU on individual and consolidated financial statements and related reports.

We do not discuss the provisions that do not constitute a real change to the present situation, but merely make the existing provisions more specific. We also do not discuss the provisions that solely concern the public sector (municipalities, towns and higher territorial units, state budget-funded and subsidized organizations).

Changes effective from 1 July 2015

Description	Previous legislation	New legislation	Substance of change
Definition of a participating interest (Article 2 (4) (m))	<p>The term "participating interest" is not defined in the Act. It is defined in the Decree on Financial Statements of Large Accounting Entities and Public-Interest Entities as follows: a participating interest shall be defined as the existence of a minimum of 20-percent ownership interest in share capital of another accounting entity (Article 5 (1) (e)). It is defined in the same manner in the Decree on Financial Statements of Small Accounting Entities (Article 5 (e)).</p> <p>The definition of a participating interest is followed by the definition of an associated accounting entity in the Decree on Financial Statements of Large Accounting Entities and Public-Interest Entities (Article 5 (1) (f)) and in the Decree on Financial Statements of Small Accounting Entities (Article 5 (f)): an associated accounting entity shall be defined as an accounting entity</p> <ul style="list-style-type: none"> - in which another accounting entity holds a participating interest and 	<p>Participating interest shall be defined as at least a 20-percent ownership interest in share capital of another accounting entity, which is held to create a durable link with that other accounting entity for the purpose of contributing to the activities of the accounting entity.</p> <p>Based on the amendment to the Act on Accounting, Article 27 of the Act has been rewritten, with the definition of a significant influence referred to in the definition of an associated accounting entity being left out. This means that a significant influence is currently not defined.</p>	<p>The change in the definition of a participating interest aims to bring it closer to the definition of participating interests in Article 2 of Directive No. 2013/34/EU. In the Directive, however, the limit of 20% is considered a (rebuttable) assumption of a participating interest, rather than being automatically considered a participating interest. This means that, in certain cases, this may be more than 20%, but, nonetheless, it will not constitute a participating interest, or, vice versa, it may be less than 20%, but it will nonetheless constitute a participating interest. Such cases occur very rarely in practice.</p> <p>Let us stress that the definition of a participating interest refers to ownership interests in share capital, rather than voting rights.</p> <p>Another change to the accounting legislation will apparently be necessary to define a significant influence. In Article 27 (1) (a) of the Act, a significant influence was previously defined as a minimum of 20% of voting rights. This definition was quite simplified and was</p>

	<ul style="list-style-type: none"> - over which that other accounting entity exercises a significant influence according to Article 27 (1) (a) of the Act. 		not entirely consistent with the Directive. However, cases where an accounting entity holds a minimum of 20% of voting rights and, in spite of this, does not have at least a significant influence occur very rarely in practice.
Classification of accounting entities into size groups (Article 2 (10))	<p>Depending on whether or not the criteria of size (net turnover, assets, number of employees) were exceeded, accounting entities were classified into the following size groups:</p> <ul style="list-style-type: none"> - a micro-accounting entity, - a small accounting entity, or - a large accounting entity. 	An accounting entity that does not meet the conditions for being classified into size groups shall be classified as a small accounting entity.	The Act responded to the situation of accounting entities where the fulfillment of the criteria of size could not be identified . Now, the Act directly determines the procedure that could be derived only indirectly prior to the amendment - an accounting entity will be classified as a small accounting entity.
Classification of accounting entities into size groups after they enter into liquidation or declare bankruptcy (Article 2 (10))	Classification of an accounting entity following its entry into liquidation or a declaration of bankruptcy is not regulated.	An accounting entity shall not change its classification into a size group after entering into liquidation or declaring bankruptcy.	An accounting entity should be classified into the size group in which it was classified before entering into liquidation or declaring bankruptcy.
Accounting entries (Article 11 (3))	Accounting entities may not make accounting entries outside their accounting books.	An accounting entity may not make accounting entries outside its accounting books, make an accounting entry on an accounting transaction that has not been carried out, and conceal or fail to account for facts subject to accounting.	As stated in the Explanatory Report, this change is in response to the OECD finding that, following the last amendment to Article 38 of the Act on Accounting, where fines related to accounting were reduced, the Slovak Republic ceased to comply with Article

			<p>8 of the Convention on combating bribery of foreign public officials in international business transactions, with sanctions for erroneous accounting failing to be effective, adequate, and deterring.</p> <p>See also the amendment to Article 38 on fines.</p>
<p>Signing of financial statements, date of their preparation (Article 17 (5) and (8))</p>	<p>The financial statements are considered to be prepared after the signatures are added to the information required according to paragraph 2 and to the individual parts of the financial statements.</p> <p>The financial statements shall be signed by the statutory body.</p>	<p>The prepared financial statements must include the signature of the statutory body.</p> <p>The date of preparation of the financial statements shall be determined by the accounting entity itself.</p>	<p>This only makes the existing provisions more specific, without any changes in terms of substance.</p>
<p>Provisions on fines – failure to maintain accounting books, failure to prepare financial statements (Article 38)</p>	<p>A failure to prepare financial statements carries a fine of up to 1,000,000 euros (Article 38 (1) (a), Article 38 (2) (a)).</p>	<p>A failure to maintain accounting books according to Article 4 (1) (= from the date of incorporation of the accounting entity to the date of its dissolution) and a failure to prepare financial statements carry a fine of up to 3,000,000 euros (Article 38 (1) (a) and (o), Article 38 (2) (a)).</p> <p>There is also a fine of up to 3,000,000 euros for the violation of the provisions of Article 11 (3) on accounting entries.</p>	<p>If an accounting entity prepares financial statements, the highest possible penalty can be up to 2% of its assets, up to a maximum of 1,000,000 euros (Article 38 (2) (b)). It is the same as up until now - a fine is up to 2% of assets, with fines of a maximum of 1,000,000 euros for certain offenses, a maximum of 100,000 euros for other offenses, and a maximum of 1,000 euros for others.</p> <p>However, if an accounting entity does not prepare financial statements, the</p>

Transitional provisions: proceedings referred to in Article 38 that commenced prior to 1 July 2015 shall be subject to legislation effective until 30 June 2015 (Article 39I).

possibility of imposing a fine of up to 2% of its assets does not exist (there is no way to ascertain the amount of its assets), and the highest possible fine was 1,000,000 euros up until now. This fine has now been increased to a maximum of 3,000,000 euros.

A fine for:

- **a failure to maintain accounting books** according to Article 4 (1) and
- for the violation of the provisions of Article 11 (3) on **accounting entries** amounts to a maximum of 3,000,000 euros. It is not quite clear whether this fine may be imposed regardless of whether or not the accounting entity prepares financial statements (what will be the connection with fines related to the provisions of Article 38 (1) (g) and (h) – if the accounting entity failed to maintain accounting books according to Article 8 and this violation had/did not have an impact on the presentation of facts in the financial statements?)

This is in response to the OECD finding; see above regarding accounting entries (Article 11 (3)).

Changes effective from 1 January 2016

Description	Previous legislation	New legislation	Substance of change
Income statement forming part of interim financial statements (Article 18 (4))	<p>The income statement forming part of interim financial statements contained expenses and income:</p> <ul style="list-style-type: none"> - with respect to the presented part of the accounting period, - aggregate information from the beginning of the year. <p>For example, if the income statement was prepared for the second quarter, it contained expenses and income:</p> <ul style="list-style-type: none"> - for the period of April-June, as well as - aggregate information for the period of January-June. <p>And by analogy with respect to a comparable accounting period.</p>	<p>The income statement forming part of interim financial statements only contains aggregate information on expenses and income from the beginning of the year.</p> <p>And by analogy with respect to a comparable accounting period.</p>	<p>Presentation of expenses and income. This change makes sense if it is not necessary to separately present expenses and income with respect to individual quarters of the year (or months), but it is sufficient to present aggregate information from the beginning of the year.</p>
Annual report – description of internal control and risk management systems (Article 20 (6) (d))	<p>It is required that an annual report of issuers of securities that were permitted to be traded on a regulated market also contain, in addition to other information, a description of internal control and risk management systems.</p>	<p>It is required to provide a description of the main internal control and risk management systems in relation to the financial statements.</p> <p>This provision also applies to a consolidated annual report (Article 22 (16)).</p>	<p>It is not required to provide a description of all internal control and risk management systems, but only:</p> <ul style="list-style-type: none"> - the main ones, - and only those that relate to the financial statements. <p>This ensures consistency with Article 20 (1) (c) of Directive 2013/34/EU.</p>

			<p>Transitional provisions: An accounting entity whose accounting period is a financial year shall prepare an annual report and a consolidated annual report for the first time with respect to the financial year that begins during the course of 2016 (Article 39m (2)). This indirectly suggests that an accounting entity whose accounting period is a calendar year should apply the new legislation with respect to the preparation of an annual report and a consolidated annual report prepared for the accounting period beginning on 1 January 2016.</p>
<p>Annual report - audit (Article 20 (3), Article 22 (2))</p>	<p>An auditor audits the consistency of the annual report with the financial statements (Article 20 (1)).</p> <p>This provision also applies to a consolidated annual report (Article 22 (16)).</p>	<p>An auditor must (Article 20 (3)):</p> <ul style="list-style-type: none"> a) express an opinion as to whether the annual report is consistent with the financial statements, b) express an opinion on information referred to in paragraph 6 (d) and paragraph 7 (c) to (e), (g), and (h) – a description of the main internal control and risk management systems in relation to the financial statements, information on qualified participation in share capital according to special legislation, the holders of any securities with special control 	<p>The provisions of (b) to (e) are new; they have been implemented from Article 34 (1), Article 20 (3), and Article 20 (1) (a), (b), (e) and (f) of Directive 2013/34/EU.</p>

rights and a description of those rights, any restrictions on those rights, the rules governing the appointment and dismissal of members of the statutory body and the amendment to the articles of association, the powers of the statutory body, and in particular the powers to decide to issue shares or buy back shares,

- c) express an opinion as to whether the annual report contains information according to special legislation,
- d) express an opinion as to whether the annual report contains information according to this Act,
- e) state whether, in the light of the knowledge of the accounting entity and its situation, the auditor has identified material misstatements in the annual report, and give an indication of the nature of any such misstatements.

These provisions also apply to a **consolidated** annual report (Article 22 (2)).

Report on payments to governments (Article 20a, Article 20b)

A report on payments to governments is not required.

A **large** accounting entity that is a **company** and a **public-interest entity** active in

- the extractive industry or
- the logging of primary forests

shall prepare and make public an annual report on payments to public authorities.

The Act specifies the extractive industry, the logging of primary forests, a public authority etc. in more detail.

Payments broken down by types and countries, whose amount exceeds 100,000 euros, should be indicated separately in the report. Payments should be presented in the structure prescribed by the Act.

If the parent accounting entity prepares a report on payments and includes payments of its subsidiary accounting entities in its report, these entities do not have to prepare a separate report.

An accounting entity that is required to prepare consolidated financial statements is also required to prepare a **consolidated report on payments** (Article 22 (2), (19), (20)).

These requirements are new, resulting from Articles 41 to 46 of Directive No. 2013/34/EU.

It is stated in Sections 44 to 49 of the Preamble to the Directive that the report should include types of payments comparable to those disclosed by an undertaking participating in the **Extractive Industries Transparency Initiative** (EITI). These reports are expected to help governments of resource-rich countries to implement the EITI principles and criteria and account to their citizens for payments that such governments receive from these undertakings.

The Act on Accounting refers to this report as a "report on payments to public authorities" (Article 20a) or a "report on payments" (Article 20a (1), Article 20b), as well as a "consolidated report on payments" (Article 20a (1), Article 22 (2), (19), (20)).

Transitional provisions: An accounting entity whose accounting period is a **financial year** shall prepare a report on payments and a consolidated report on payments for the first time with respect to the financial year that begins during the course of 2016 (Article 39m (2)). This indirectly

		<p>The report does not have to be audited by an auditor.</p> <p>Report on payments to governments is included in the annual report (Article 22 (2)).</p>	<p>suggests that an accounting entity whose accounting period is a calendar year should prepare these reports for the first time with respect to the accounting period beginning on 1 January 2016.</p>
<p>Consolidated financial statements – another possibility of exemption from the obligation to prepare consolidated financial statements (non-inclusion of subsidiary accounting entities under the full consolidation method); (Article 22 (13))</p>	<p>All parent accounting entities are required to prepare consolidated financial statements. There are three situations where a parent accounting entity is exempted from this obligation:</p> <ul style="list-style-type: none"> - an intermediate parent company within a group (Article 22 (8), (9), (11)), - by reason of not exceeding the criteria of size (Article 22 (10), (11), - by reason of immateriality of subsidiary accounting entities (Article 22 (12)). <p>Exemption for an intermediate parent company within a group and exemption by reason of immateriality of subsidiary accounting entities are referred to as mandatory in the Fourth Directive (predecessor of the current Directive No. 2013/34/EU), which is why Member States had to implement them.</p> <p>Exemption by reason of not exceeding the criteria of size is referred to as optional in the Fourth Directive,</p>	<p>Another situation has been added to these three situations – if a parent accounting entity only has such subsidiary accounting entities that do not have to be included in consolidated financial statements under the full consolidation method. This applies if they meet at least one of the following conditions (Article 22 (13)):</p> <ul style="list-style-type: none"> a) long-term restrictions exist that severely hinder the parent accounting entity in the exercise of its rights over the assets of the subsidiary accounting entity or its rights over management of the subsidiary accounting entity, b) information necessary for the preparation of consolidated financial statements can only be obtained with disproportionately high expense or excessive delay, or c) the parent accounting entity holds an ownership interest in the subsidiary accounting 	<p>This provision has been implemented from Article 23 (10) (b) (as well as from the related paragraph 9) of Directive No. 2013/34/EU. In these cases, the Directive – in contrast to the IFRS – makes it possible (= optional) to not include these subsidiary accounting entities in the consolidated financial statements under the full consolidation method. And since the test to see whether the parent accounting entity is required to prepare consolidated financial statements is carried out according to the Directive, rather than the IFRS, the provisions of the Directive, rather than those of the IFRS, are relevant to the purpose of this test.</p> <p>The terms "long-term restrictions," "severely", "disproportionately high expense," and "excessive delay" are not defined - either in the Act or the Directive.</p> <p>Transitional provisions: A parent accounting entity shall prepare consolidated financial statements</p>

	<p>which is why Member State may have implemented them, but did not have to do so. The Slovak Republic implemented this reason and partially modified it.</p>	<p>entity solely for the purpose of its sale.</p>	<p>according to Article 22 in the wording effective from 1 January 2016 for the first time with respect to the financial year that begins during the course of 2016 (Article 39m (3)). This indirectly suggests that if its accounting period is a calendar year, it should prepare consolidated financial statements according to these amended provisions for the first time with respect to the accounting period beginning on 1 January 2016.</p> <p>If applied to our case, the term "shall prepare consolidated financial statements for the first time" means "shall apply this test for the first time."</p>
<p>Consolidated financial statements – exemption for an intermediate parent company within a group – prohibition of exemption (Article 22 (8), (9) and (11))</p>	<p>If an accounting entity is a parent accounting entity (i.e., there is a subsidiary accounting entity "under it") and is at the same time a subsidiary accounting entity (i.e., it has a parent accounting entity "above it"), it is a so-called intermediate parent company within a group. Under certain circumstances, it is exempted from the obligation to prepare consolidated financial statements (Article 22 (8), (9) and (11)).</p> <p>However, this exemption does not apply to cases (= prohibition of exemption) where an accounting entity</p>	<p>Prohibition of exemption from the obligation to prepare consolidated financial statements applies not only to cases where a parent accounting entity is an issuer of securities (as has been the case up until now), but it has been extended to cases where a parent accounting entity is a public-interest entity or any of its subsidiary accounting entities is a public-interest entity (Article 22 (11), first sentence).</p>	<p>This is an inaccurate implementation of Article 23 (3) of Directive No. 2013/34/EU. According to the Directive, the prohibition of exemption from the obligation to prepare consolidated financial statements only applies to issuers of securities (as has been the case up until now), and Member States must not expand it. Therefore, this provision of the Act on Accounting should have remained unchanged.</p> <p>Transitional provisions: see above, they are common to all changes concerning consolidated financial statements (Article 39m (3)).</p>

	<p>issued securities that were permitted to be traded on a regulated market of a Member State or a state of the European Economic Area (Article 22 (11), last sentence).</p>		
<p>Consolidated financial statements – exemption by reason of not exceeding the criteria of size – prohibition of exemption (Article 22 (11))</p>	<p>A parent accounting entity is not required to prepare consolidated financial statements if the criteria of size are not exceeded (Article 22 (10)).</p> <p>This exemption does not apply to cases (= prohibition of exemption) where a parent accounting entity or any of its subsidiary accounting entities issued securities that were permitted to be traded on a regulated market of a Member State or a state of the European Economic Area (Article 22 (11), first sentence).</p>	<p>The prohibition of exemption has been repealed.</p>	<p>This is an inaccurate implementation of Article 23 (1) of Directive No. 2013/34/EU.</p> <p>According to this Article, this exemption does not apply to cases (= prohibition of exemption) where a parent accounting entity or any of its subsidiary accounting entities is a public-interest entity.</p> <p>The Act on Accounting therefore should not have repealed this prohibition, but, on the contrary, it should have extended it to other public-interest entities. Issuers of securities are only a subset of public-interest entities. Public-interest entities are defined in Article 2 (14) of the Act and include not only issuers of securities, but also banks, insurance companies, large companies, and so forth.</p> <p>Transitional provisions: see above, they are common to all changes concerning consolidated financial statements (Article 39m (3)).</p>

Consolidated financial statements – criteria of size (Article 22 (10), (11))

There are three criteria of size (Article 22 (10):

- assets (net): 17,000,000 euros,
- net turnover: 34,000,000 euros,
- the average recalculated number of employees: 250.

The criteria of size should be added up from the individual financial statements of the parent accounting entity and all its subsidiary accounting entities. In so doing, **intra-group relations are not eliminated** (mutual receivables and liabilities, expenses and income arising from mutual transactions, financial investment against equity, subtotal).

This means that only a simple arithmetic total is calculated.

A parent accounting entity is exempted from the obligation to prepare consolidated financial statements if at least two of these criteria **are not exceeded** for two successive accounting periods.

The three criteria of size continue to exist, and an **accounting entity may choose** to determine them **before** or **after** the elimination of intra-group relations.

If the accounting entity chooses to do so **after the elimination**, the criteria are as follows:

- assets (net): 20,000,000 euros,
- net turnover: 40,000,000 euros,
- the average recalculated number of employees: 250.

If the accounting entity chooses to do so **before the elimination**, the criteria regarding assets (net) and net turnover will be increased by 20% and will amount to the following:

- assets (net): 24,000,000 euros,
- net turnover: 48,000,000 euros,
- the average recalculated number of employees: 250.

When determining the criteria of size, **information** related to those subsidiaries that **do not have to be included** in the consolidated financial statements **under the full consolidation method** (see above)

This is an implementation of the provisions of Article 3 and Article 23 (1) and (2) of Directive No. 2013/34/EU. Not only **small groups** of accounting entities are mandatorily exempted from the obligation to prepare consolidated financial statements (the criteria are: 4,000,000 – 8,000,000 – 50), but the Slovak Republic also used the possibility (= option) of exempting **medium-sized groups** of accounting entities (the criteria are: 20,000,000 – 40,000,000 – 250) as well.

It is still not stipulated whether or not immaterial subsidiary accounting entities should also be included in the total sum.

Transitional provisions: see above, they are common to all changes concerning consolidated financial statements (Article 39m (3)).

		<p>should not be considered. They should not be included in the total sum (Article 22 (11) (a)).</p> <p>It continues to apply that a parent accounting entity is exempted from the obligation to prepare consolidated financial statements if at least two of these criteria are not exceeded for two successive accounting periods.</p>	
<p>Deadline for filing approved financial statements in the register of financial statements (Article 23a)</p>	<ul style="list-style-type: none"> - Neither the time limit for the approval of the financial statements by the general meeting - nor the time limit for filing the approved financial statements in the register of financial statements are stipulated. <p>The statutory body of a limited liability company and a joint stock company must present the individual financial statements to the general meeting for approval within 6 months from the end of the accounting period (Article 40 (1) of the Commercial Code), but the time limit for its approval by the general meeting is not stipulated.</p> <p>If the financial statements are approved, a notification on the date of approval should be filed in the register of financial statements (Article 23a (4)).</p>	<p>An accounting entity must file the approved financial statements or a notification on the date of approval of the financial statements in the register at the latest within one year of the end of the accounting period for which the financial statements are prepared (Article 23a (7)).</p>	<p>This time limit is stipulated in Article 30 (1) of Directive No. 2013/34/EU.</p>

Cancellation of valuation at replacement cost (Article 25 (1) (d))

As of the **date of the accounting transaction** (Article 24 (1) (a)), i.e., as of the date of acquisition/self-construction (= **as of the date of initial recognition**) the following should be valued at the replacement cost (Article 25 (1) (d)):

1. assets acquired free of charge, except for cash, stamps and vouchers, and receivables valued at their nominal value,
2. internally generated intangible assets if the conversion cost of these assets exceeds their replacement cost,
3. livestock if the conversion cost cannot be determined,
4. assets transferred from personal ownership to the business, except for cash, stamps and vouchers, and receivables valued at their nominal value,
5. intangible assets, property, plant and equipment and inventories newly identified during the reconciliation procedures, which are not recorded in the accounting books,
6. assets acquired by a public procurer free of charge from a concessionaire for a supply in the form of a concession for a construction work project according to special legislation.

Valuation at replacement cost has been repealed. Valuation at **fair value** should instead be used.

Fair value should be used for valuation in the cases referred to in points 1, 4, 5, and 6.

The remaining points – 2 and 3 – have been **repealed without replacement**. It is therefore not quite clear how these cases should be valued.

- In the case of intangible assets, the actual cost will apparently be used and a value adjustment will be created.
- In the case of livestock, it will apparently be necessary to make an estimate of the conversion cost.

The definition of the replacement cost in Article 25 (6) (b) has been repealed.

This change has resulted from Directive No. 2013/34/EU, which repealed the possibility of using replacement cost as a valuation quantity, considering fair value to be one of the possibilities of replacing it.

Transitional provisions: An accounting entity whose accounting period is a **financial year** shall value its assets according to Article 25 (1) (d) (= fair value as a replacement for the replacement cost) in the wording effective from 1 January 2016 for the first time with respect to the financial year that begins during the course of 2016 (Article 39m (1)). This indirectly suggests that an accounting entity whose accounting period is a **calendar year** should apply the new legislation for the first time with respect to the accounting period beginning on 1 January 2016.

Definition of the acquisition cost (Article 25 (6) (a))	<p>Acquisition cost shall be defined as the price at which an asset has been acquired plus costs related to the acquisition.</p>	<p>Acquisition cost shall be defined as the price at which an asset has been acquired plus costs related to the acquisition and all reductions in the acquisition cost.</p>	<p>This makes the definition more specific, so that it is clear that any possible credit notes, discounts, early payment discounts and so forth reduce the acquisition cost.</p>
Valuation of securities and ownership interests available for sale (Article 25 (8))	<p>Upon initial recognition, securities and ownership interests available for sale shall be valued at their acquisition cost (Article 25 (1) (a) (3)).</p>	<p>Securities available for sale may (= optional) be valued at their acquisition cost or fair value,</p> <ul style="list-style-type: none"> - both upon initial recognition, and - as of the balance sheet date, i.e., in the financial statements. <p>This means that an accounting entity can choose to value them at their acquisition cost or at their fair value.</p> <p>However, if the accounting entity does not value them at their fair value upon initial recognition (for example, acquisition), it also cannot value them at their fair value as of the balance sheet date (Article 27 (10)).</p> <p>In other words, if the accounting entity values them at their acquisition cost upon initial recognition, it cannot value them at their fair value in the financial statements. And if it values them at their fair value upon initial recognition, it must also value them at their fair value in the financial statements.</p>	<p>The Explanatory Report says that the term "securities and ownership interests available for sale" is also referred to by using the technical term "short-term available-for-sale securities and ownership interests."</p> <p>This indirectly transpires from the classification of securities and ownership interests according to Article 14 (7) of the Accounting Procedures for Entrepreneurs.</p> <p>As this provision will enter into force on 1 January 2016, it will not be possible to value securities and ownership interests available for sale, which were acquired prior to that date, at their fair value - nor in the financial statements prepared after 1 January 2016.</p>

Fair value – definition (Article 27)

Fair value **is not defined**. This means that there is no **general** definition, for example, such as that contained in IFRS 13 Fair Value Measurement: Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Fair value **is still not generally defined**.

Directive 2013/34/EU also does not provide any **general definition** of fair value. To understand the basis of the reworked Article 27, certain terms referred to in the Directive are described below.

The Directive does not define fair value in general. Article 8 (7) only stipulates that the fair value must be determined (= **obligatory**) by reference to one of the following values:

- a **market value**, for those financial instruments for which a reliable market can readily be identified. Where a market value is not readily identifiable for an instrument but can be identified for its components or for a similar instrument, the market value may be derived from that of its components or of the similar instrument;
- a **value resulting from generally accepted valuation models and techniques**, for those instruments for which a reliable market cannot be readily identified, provided that such valuation models and techniques ensure a reasonable approximation of the market value.

			<p>In addition, the Directive refers to the following terms:</p> <ul style="list-style-type: none"> - revalued amount, (Article 7), at which fixed assets may be valued, - amount determined by reference to fair value (Article 8 (1) (b)), which may be used to value assets other than financial instruments. <p>The Directive does not define either of these terms.</p>
<p>Fair value – valuation upon initial recognition and as of the balance sheet date (Articles 24, 25, and 27)</p>	<p>Fair value is used for the valuation of assets and liabilities:</p> <ul style="list-style-type: none"> - as of the date of the accounting transaction (initial recognition), Article 25, Article 24 (1) (a)), - as of the balance sheet date, i.e., in the financial statements (Article 27 (1), Article 24 (1) (b)). <p>The aforementioned paragraphs set out specific asset and liability items that should be valued at their fair value.</p> <p>If fair value cannot be reliably determined as of the valuation date, valuation under the methods specified in Article 25 (i.e., acquisition cost, conversion cost, nominal value) shall be considered the fair value; Article 27 (9), first sentence.</p>	<p>Nothing has been changed about this principle.</p> <p>However, the list of assets and liabilities that should be valued at their fair value as of both dates has been changed.</p> <p>Upon initial recognition:</p> <ul style="list-style-type: none"> - fair value has replaced replacement cost (see above, Article 25 (1) (d)), - fair value may be used to value securities and ownership interests available for sale (see above, Article 25 (8)). <p>In the financial statements, the following items have been added to the list:</p>	<p>See left.</p> <p>Transitional provisions: An accounting entity whose accounting period is a financial year shall value its assets and liabilities according to Article 27 in the wording effective from 1 January 2016 for the first time with respect to the financial year that begins during the course of 2016 (Article 39m (1)). This indirectly suggests that an accounting entity whose accounting period is a calendar year should apply valuation at fair value according to the new legislation for the first time with respect to the accounting period beginning on 1 January 2016.</p>

		<ul style="list-style-type: none"> - liabilities included in the portfolio of financial instruments held for trading (Article 27 (1) (i)), - securities and ownership interests available for sale (see above, Article 25 (8)), <p>and the following item has been deleted from the list:</p> <ul style="list-style-type: none"> - real estate in which funds of technical provisions are placed and technical provisions with respect to accounting entities that are insurance companies or reinsurance companies according to special legislation (reference to Act No. 95/2002 on the Insurance Sector). Nonetheless, these accounting entities prepare their financial statements according to the IFRS, rather than according to Slovak accounting legislation. <p>It continues to apply that if fair value cannot be reliably determined, valuation at fair value shall not be made (Article 27 (12)).</p>	
<p>Fair value – what is understood as fair value (Article 27)</p>	<p>Fair value shall be defined as (Article 27 (2)):</p> <ul style="list-style-type: none"> a) the market price (active market, decisive regulated market), 	<p>Fair value shall be defined as (Article 27 (2)):</p> <ul style="list-style-type: none"> a) the market price (active market, decisive regulated market), 	<p>The new provisions are more structured and sophisticated.</p> <p>One of the changes is that, the new provisions place greater emphasis on</p>

- b) the valuation on the basis of a **professional estimate** or **expert opinion** if the market price is not available or does not appropriately express the fair value,
- c) the valuation defined in **special legislation** (reference to the Act on Collective Investment) if it is not possible to proceed according to (a) and (b),
- d) the **value of the work project performed**, provided by a concessionaire to a public procurer, for which the concessionaire acquires intangible assets referred to in Article 25 (1) (g).

In certain cases, a professional estimate shall also be deemed to include **other expert estimates** (Article 27 (7)).

It transpires from the above that **the accounting entity itself** may also determine fair value if it is not the market price or if an expert opinion is not required.

- b) a value resulting from a **valuation model** predominantly based on information on operations or quotations in an **active market** if the price referred to in (a) is not available,
- c) a value resulting from a **valuation model** predominantly based on information on operations or quotations in **other than an active market** if there is no information available in an active market that could be used in the valuation model referred to in (b), or
- d) an **expert opinion** if the fair value of an asset item subject to valuation cannot be determined according to (a) to (c), **or** where no valuation model is available for an item subject to valuation to estimate in an adequately reliable manner the price of an asset at which it would be **sold** at the given time, or where its use would require disproportionate effort or expense on the part of the accounting entity in proportion to the benefits of its use for the quality of the presentation of the accounting

the **sale**, which can be seen in the provisions of (d) ... "the price of an asset at which it would be **sold** at the given time ...".

The Explanatory Report says the following:

A new wording of Article 27 has been stipulated. The reason is to define valuation at fair value in such a way that **it can always be obtained** and that it is not necessary to value an individual asset at its acquisition cost in a certain accounting period solely because fair value is not available.

The application of **valuation models** that are suitable to estimate fair value has been stipulated for this purpose.

An **accounting entity may create its own** model based on professional literature describing the modeled item, its knowledge of the modeled item, and the principles of mathematical modeling. Or it may purchase a valuation model, for example, from a consulting company.

The **complexity of a model** should correspond to the complexity of an asset whose valuation is estimated.

- For example, in the case of

		<p>entity's financial position in the financial statements.</p> <p>Valuation models shall be based on (Article 27 (7)):</p> <ul style="list-style-type: none"> - the market approach, - the cost approach, with this approach being used primarily to value non-financial assets, - the income approach. 	<p>valuation of options, relatively complex option models are used, such as the Black-Scholes-Merton model or the binomial model.</p> <ul style="list-style-type: none"> - For the valuation of assets identified during reconciliation procedures, it will suffice to use a simple model created on the basis of the cost approach. This means the most advantageous purchase price from the viewpoint of the accounting entity performing the valuation (distance from the seller, product parameters that are closest to the product subject to valuation), adjusted by the extent of wear and tear of the product. <p>In the case where none of the models is suitable for the valuation of a specific asset item, an expert opinion should be used.</p> <p>Transitional provisions: see above.</p>
<p>Equity method (Article 27 (8))</p>	<p>The equity method may (= optional) be used for the valuation of ownership interests in share capital of subsidiary and associated accounting entities.</p>	<p>The equity method may (= optional) be used for the valuation of shares and ownership interests in a subsidiary accounting entity and an</p>	<p>This is an approximation of Article 9 (7) of Directive No. 2013/34/EU. According to the Directive, this method may also be used for the valuation of a</p>

If the accounting entity uses this method, it is required to use the same method for the valuation of **all** such shares (Article 27 (9)).

The **procedure** under the equity method is specified in Article 14 (18) of the Accounting Procedures for Entrepreneurs.

accounting entity with a participating interest.

It continues to apply that if the accounting entity uses this method, it is required to use the same method for the valuation of **all** such shares, provided that it can determine their value using the equity method.

For an accounting entity in which another accounting entity holds a participating interest, the **obligation** has been established to **provide information** on the current structure of its equity at such a time that the other accounting entity could use the equity method.

The **procedure** under the equity method is now specified in the Act as well, and not only in the Accounting Procedures for Entrepreneurs.

participating interest; it does not refer to subsidiary accounting entities. In practice, however, subsidiary accounting entities are a subset of participating interests in most cases; but this may not always be the case, and such cases would go beyond the scope of the Directive.

It continues to apply that it is **optional** to use the equity method.

While this method applied to ownership interests in subsidiary and associated accounting entities up until now, following the amendment, it applies to ownership interests in subsidiary accounting entities and accounting entities with a participating interest, which is not the same thing. As a rule, however, there will be no differences in practice, because, in most cases, if an accounting entity holds a 20%-ownership interest in share capital of another accounting entity (= has a participating interest), then the other accounting entity is, at a minimum, its associated accounting entity.

Transitional provisions: the same as those applicable to fair value; see above.

Amortization of goodwill and capitalized development costs (Article 28 (4))

Goodwill shall be amortized during the expected period of use corresponding to the consumption of future economic benefits.

Capitalized **development costs** should be amortized in the same way, but they must be written off within five years from their acquisition.

If **development costs have not been fully amortized**, an accounting entity may pay out dividends, profit shares, and royalties only if the total amount of net profit/net loss and funds created from profit intended for payment (= on the liability side, in equity) exceeds the total amount of unamortized development costs (= on the asset side). This is the so-called "**prevention**" against distribution of equity.

If the useful life of goodwill and capitalized development costs **cannot be reliably estimated**, they must be written off within **five years** from their acquisition.

The "**prevention**" **continues to apply** - if capitalized development costs have not been completely written off, an accounting entity may distribute profit only if the total amount of reserve funds and other equity components available for payment exceeds the total amount of unamortized capitalized development costs.

These provisions have been implemented from Article 12 (11) of Directive No. 2013/34/EU.

This regulates a situation where the useful life of goodwill and capitalized development costs **cannot be reliably estimated**. This situation will occur in practice only in exceptional cases.

Until now, **development costs** had to be written off within five years from their acquisition, whereas it will now be possible to amortize them for **longer than five years**.

The provisions regarding the "prevention" have been made more specific.

Transitional provisions: The provisions of Article 28 (4) in the wording effective from 1 January 2016 shall be applied to goodwill and capitalized development costs **acquired from 1 January 2016** (Article 39m (4)).

This means that goodwill and capitalized development costs **acquired prior to that date** should be amortized according to the previous legislation.

Changes effective from 1 January 2017

Description	Previous legislation	New legislation	Substance of change
Annual report – corporate social responsibility area (Article 20 (9) to (12), (15))	<p>Requirements concerning the disclosure of information regarding corporate social responsibility (CSR) are limited to the following:</p> <ul style="list-style-type: none"> - important financial and non-financial indicators, including information about the impact of the accounting entity's activities on the environment and on employment (Article 20 (1) (a)). <p>This information should be disclosed in an annual report of all accounting entities that are required to prepare an annual report.</p>	<p>Article 20 (9): A public-interest entity whose average recalculated number of employees exceeds 500 during the accounting period shall include in its annual report non-financial information on the accounting entity's development, performance, position and impact of its activity on environmental, social and employee matters, information on respect for human rights, and information on anti-corruption and bribery matters. The Act lists information that needs to be disclosed.</p> <p>It is possible to rely on various international frameworks; the Act does not refer to any specific frameworks.</p> <p>By disclosing information referred to in paragraph 9, the obligation to disclose non-financial information on the impact of the accounting entity's activities on the environment and employment according to paragraph 1 (a) shall be deemed to have been fulfilled.</p> <p>A subsidiary accounting entity does not have to disclose information</p>	<p>These are new requirements resulting from Directive 2014/95/EU amending Directive 2013/34/EU.</p> <p>The Explanatory Report gives examples of international frameworks that can be relied upon, for example, the Eco-Management and Audit Scheme (EMAS), the UN Global Compact initiative, the Guiding Principles on Business and Human Rights implementing the UN "Protect, Respect and Remedy" Framework, the OECD Guidelines for Multinational Enterprises, the International Organization for Standardization's ISO 26000, the International Labor Organization's Tripartite Declaration of principles concerning multinational enterprises and social policy, the Global Reporting Initiative, or other recognized international frameworks.</p> <p>Transitional provisions: Unlike the provisions entering into force on 1 January 2016, there are no transitional provisions regarding the provisions entering into force on 1 January 2017. However, if we were to proceed by analogy (Article 39m (2)), then an</p>

		<p>referred to in paragraph 9 if information on that entity and all its subsidiary accounting entities is included in the annual report or similar report of the parent accounting entity.</p> <p>If an accounting entity does not disclose information referred to in paragraph 9, it shall include in its annual report a clear and reasoned explanation of the reasons for not doing so.</p> <p>These provisions also apply to a consolidated annual report (Article 22 (16)).</p>	<p>accounting entity whose accounting period is a financial year should apply the new legislation for the first time with respect to the preparation of an annual report and a consolidated annual report for the financial year that begins during the course of 2017. An accounting entity whose accounting period is a calendar year should apply the new legislation with respect to the preparation of an annual report and a consolidated annual report for the accounting period beginning on 1 January 2017.</p>
<p>Annual report – description of the diversity policy (Article 20 (13) and (14))</p>	<p>Information on the diversity policy is not required.</p>	<p>An issuer of securities that were permitted to be traded on a regulated market of any Member State, which meets at least two of the following conditions as of the balance sheet date:</p> <ul style="list-style-type: none"> - its assets (net) exceeded 20,000,000 euros, - its net turnover exceeded 40,000,000 euros, - its average recalculated number of employees exceeded 250, <p>shall also include in its annual report a description of the diversity policy applied in relation to its administrative, management, and supervisory bodies,</p>	<p>These are new requirements resulting from Directive 2014/95/EU amending Directive 2013/34/EU.</p> <p>Transitional provisions: None; see above.</p>

primarily with regard to the age, gender, and educational and professional backgrounds of members of these bodies, the objectives of that policy, the manner in which it has been implemented, and the results achieved in the reported period.

If it does not disclose this information, it should include in its annual report the reasons for which it has decided not to apply the diversity policy.

These provisions also apply to a **consolidated** annual report (Article 22 (16)).

Abbreviations:

- Decree of the Finance Ministry of the Slovak Republic No. 23054/2002-92 as amended laying down details of the accounting procedures and the framework for the chart of accounts for entrepreneurs maintaining accounts under the system of double entry bookkeeping ("Accounting Procedures for Entrepreneurs"),
- Decree of the Finance Ministry of the Slovak Republic No. 23378/2014-74 laying down details of individual financial statements and the extent of data contained in individual financial statements to be published by small accounting entities ("Decree on Financial Statements of Small Accounting Entities"),
- Decree of the Finance Ministry of the Slovak Republic No. 23377/2014-74 laying down details of individual financial statements and the extent of data contained in individual financial statements to be published by large accounting entities and public-interest entities ("Decree on Financial Statements of Large Accounting Entities and Public-Interest Entities").

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