



САВЕЗ РАЧУНОВОЋА И РЕВИЗОРА РЕПУБЛИКЕ СРПСКЕ
The Association of Accountants and Auditors of Republic of Srpska

19th International Congress of Accounting and Auditing Profession in the Republic of Srpska was held at Banja Vrucica, 24- 26 September 2015 under the title of:

**FINANCIAL REPORTING AND MANAGEMENT AS A FACTOR OF
SUCCESSFUL OPERATIONS**

This traditional and the most visited business gathering in the region was attended by around one thousand participants and guests from the area of former Yugoslavia and Europe. 16 scientific papers which were prepared by 22 authors were presented at the Congress and published in the Book of Papers.

After an opening remark from the chairman of the Management Board of the Association of Accountants and Auditors of Republic of Srpska, Prof. dr. Dragan Mikerevic, the Congress was opened by the Finance Minister of the Republika Srpska Government, Dr. Zoran Tegeltija. Minister Tegeltija stressed in his presentation the importance of accounting as one of the key pillars of the financial system. At this occasion he emphasized that our accounting profession has not yet achieved the status that matches its social role, however it is often the case that omissions are unduly attributable to accountants when they are not accountable for the same. In addition, the Minister informed the participants on the status of the implementation of economic policy of the Republika Srpska Government. Other presenters included the president of the Association of Authorized Auditors of Poland, Mr. Krzysztof Burnos, the president of the Association of Certified Accountants of Poland, Mr. Ryszard Gorycki and the president of the Association of Accountants and Auditors of Bulgaria, Mr. Dimitar Yordanov. The General Secretary to the Association of Accountants and Auditors of Republic of Srpska, Prof. dr. Novak Kondic on behalf of the Association of Accountants and Auditors of Republic of Srpska signed the Memorandum of understanding with the president of the Association of Authorized Auditors of Poland, Mr. Krzysztofom Burnos and with the president of the Association of Certified Accountants of Poland, Mr. Ryszardom Gorycki.

During the first day of the Congress a „roundtable“ discussion was organized at which a new book by Prof. dr. Jovan Rodic titled „Creation of sound and sustainable business environment“ was presented. The book tackles the issues of the application of a fair value concept and implications that inconsistent application of fair value may have for the country’s business



САВЕЗ РАЧУНОВОЂА И РЕВИЗОРА РЕПУБЛИКЕ СРПСКЕ

The Association of Accountants and Auditors of Republic of Srpska

environment. During the roundtable discussions, besides the author of the book, Prof. dr. Milovan Filipovic, Prof. dr. Dragan Mikerevic and Prof. dr. Kata Skaric Jovanovic also talked about the issues relating to challenges and problems of the use of a fair value concept.

During the second day of the Congress, the Banja Luka Stock Exchange director, Mr. Milan Bozic presented a system of multilateral compensation and cession in Republika Srpska, the first- time- application of which is expected over the next several days as in accordance with the Law on single system for multilateral compensation and session. Presented below are the following:



САВЕЗ РАЧУНОВОЂА И РЕВИЗОРА РЕПУБЛИКЕ СРПСКЕ
The Association of Accountants and Auditors of Republic of Srpska

CONCLUSIONS OF THE 19TH CONGRES OF AAA RS

1. Revenue generating, assets and financial position of the Republika Srpska's economy has deteriorated in 2014 as compared to 2012 and 2013 as data given below reveal:

Revenue generating position of the Republika Srpska's economy has significantly fallen when compared to 2013

- *ratio of net income returned as a percentage of shareholders equity fell from 0,9% to (0,23%)¹*
- *ratio of net income returned on fixed assets fell from 1,03% to 0,53%*

Assets position of the economy of the Republic of Srpska stagnates as shown by the following ratios:

- *operating assets turnover ratio in 2013 and 2014 was 0,52 and 0,53 respectively,*
- *fixed assets turnover ratio was 0,73 and 0,74 respectively,*
- *current assets turnover ratio fell from 1,81 to 1,77,*
- *inventory turnover ratio was 6,4 and 6,6 respectively*

Financial position of the Republika Srpska's economy in 2014 when compared to 2013 shows the following indicators:

- *missing capital in the economy of Republika Srpska for maintaining long-term financial equilibrium has increased in 2014 and amounted 2,7 billion Convertible Marks while in 2013 it amounted 2,2 billion Convertible Marks,*
- *coverage of inventories by net current assets in 2014 has deteriorated and amounted 14,5 % whereas in 2013 it amounted 32,6%.*
- *the economy's debt ratio in 2014 was 47,0% whereas in 2013 it was 44,5% and solvency decreased from 2,20 in 2013 to 2,16 in 2014.*

¹ Numbers in parentheses indicate negative amounts, in this case meaning that the economy suffered negative net equity return.



САВЕЗ РАЧУНОВОЂА И РЕВИЗОРА РЕПУБЛИКЕ СРПСКЕ

The Association of Accountants and Auditors of Republic of Srpska

The reasons for negative trends should be primarily linked to the damages caused by the flooding in a month of May and poor competitiveness of the domestic economy in the market.

2. Accountants historically have never been exposed to more complex requirements in terms of application of appropriate rules pertinent to normative accounting basis. The complexity of normative basis which incapacitates accountants to understand properly its requirements may have equally harmful implications for the quality of the financial reporting as the application of „creative accounting.“

3. The application of „mixed” normative basis adds to complexity of the financial reporting in several ways. Firstly, it combines two concepts of financial reporting, namely, concept of historical cost and a fair value concept which are mutually exclusive given their respective objectives and rules for recognition and measurement. The application of fair value concept increased the need for appropriate valuations of some balance sheet items which in turn requires specific expertise knowledge.

4. Correct application of the complex normative basis assumes that accountants understand substance of business operations and substance of transactions. Understanding of the substance of transactions and normative basis enables the accountants to select a proper way to present truly the implications of transactions in financial statements. This requires not only new, additional knowledge but also a new approach to education process in a way that it focuses on understanding as opposed to memorizing the objectives and principles, as well as on understanding the concepts of financial reporting which are embraced in normative basis.

5. Fair value is a concept resulting from the evolution of human thought on valuations. Despite numerous discussions pointing out serious issues arising from the use of fair value, the highest financial reporting authorities have decided to unreservedly support its use. The ensuing threats should be curtailed by undertaking appropriate measures meaning that the fair value concept should not be discharged but subjected to improvements in its application. Therefore it is necessary to highlight the problems arising from the use of fair value, some important weaknesses and the need for improvements which may result in higher quality measurements and more reliable financial reporting, by means of:

- fighting against manipulation of fair-value estimates;



САВЕЗ РАЧУНОВОЋА И РЕВИЗОРА РЕПУБЛИКЕ СРПСКЕ

The Association of Accountants and Auditors of Republic of Srpska

- *strengthening the role of management bodies i.e. their responsibility for the quality of fair value measurements and shifting the responsibility from a collective body to individuals performing its functions;*
- *strengthening internal controls over fair value measurements;*
- *training the auditors in fair value analysis;*
- *better shaping the role of a regulator in supervising the fair value measurements;*
- *strengthening of the appraisers profession which must be better organized and appraisal audit system should be established*

6. The extent to which independent auditors contribute to the occurrence and persistence of adverse effects of the global crisis is not negligible. *Primarily*, auditors have not, in a timely manner, pointed out uncertainties with respect to probability of a continuation of business operations (going concern) of disrupted financial institutions which only worsened already existing numerous adverse effects of the crisis. *Secondly*, a large number of inappropriately expressed audit opinions in the period prior to the onset of a crisis, especially in relation to a going concern concept constituted an additional cause to the occurrence of a crisis and its rapid development later on. *Third*, but not the least important one, is the issue of concern that the “big four” audit companies themselves for a longer period of time have been issuing positive instead of an adequate i.e. adverse opinion with respect to financial statements of significant number of their clients (clients as a rule having been the large ones).

7. Irrespective of numerous differences between functions of external and internal audit which are reflected in their different mandates, manner of organization, position with respect to legislative and executive authorities, manner and modalities of accomplishing the independence as a key determinant of each audit, the degree of development in systems undergoing transition and similar, the audit undoubtedly stands as a single profession whose key feature is working towards the protection of public interest. Intensive and continuous cooperation between these two functions based on highly standardized norms and rules of professional and ethical conduct means not only legal and professional responsibility but an absolute necessity, especially in conditions when functioning of public sector institutions is hampered with recurrent illiquidity and with numerous other, more or less unbiased and biased, reasons which affect adversely the efficiency and effectiveness of those institutions.



САВЕЗ РАЧУНОВОЂА И РЕВИЗОРА РЕПУБЛИКЕ СРПСКЕ

The Association of Accountants and Auditors of Republic of Srpska

8. Emphasis of matter paragraph in an audit report should draw attention of users to information presented in financial reports which may be significant to their decision-making. Likewise, drawing attention to issues of no fundamental significance reduces the efficiency of audit report. Drawing attention to going concern issue may be a warning sign to both the investors and creditors to monitor future operations of a company. In this way creditors could take an action on a timely basis (for example, by initiating insolvency proceedings) in order to reduce their losses i.e. losses of the economy as a whole.

9. The implementation of information technologies, above all, incurs costs regardless to the form of the information technologies that the audit companies end up selecting. It may also provoke resistance by employees due to the changes it brings. In order to ensure efficient implementation of the information technologies in audit companies it is necessary for the audit companies to understand that the information technologies are of a continuous rather than “one-off” nature. After implementing the information technologies in an audit of financial statements it is necessary to measure and analyze the performances in the process of realization of audit engagements on a continuous basis to ensure that measures are undertaken and operating goals are fulfilled on a timely basis.

10. The objective of financial statements is to present to the interested public the results of the use of resources which have been available to the entity. The true and fair presentation of financial statements is necessary given that the information presented are of great significance to shareholders, managers, employees and government. The practice in the world shows that true and fair view is often compromised. Most factors which distort the true and fair view are of *subjective nature* and only several of them are inherent limitations. Therefore auditors can find themselves in a position to express an opinion on financial statements which may not reflect the real situation. Independent auditors must put maximum efforts to express an adequate audit opinion on the financial statements of their clients in each and every audit engagement. Only in this way may the auditors restore their reputation which has been severely shaken, without a doubt, through mostly a fault of their own.

11. The complexity of both business processes and decision-making processes has increased due to economic globalization and digital economy. The increased complexity of business processes leads to greater costs and mainly to longer production times, decreased efficiency



САВЕЗ РАЧУНОВОЋА И РЕВИЗОРА РЕПУБЛИКЕ СРПСКЕ

The Association of Accountants and Auditors of Republic of Srpska

and poorer quality of operations which significantly affect business excellence and competitive position of a company. The management of a company may prevent and just as well control an overwhelming complexity. Basic purpose of streamlining business processes is to reduce costs and shorten the customer response times so to improve customer value, or summarizing in just one word, to increase the business excellence both the operational as well as the managerial one.

12. Profit variance analysis represents one of the prerequisites of a sound performance management of a company. Strategic profitability analysis enables the monitoring of the process of strategy implementation. Its purpose is both to give early warnings signs about the factors which may jeopardize strategy implementation and to identify new opportunities in the market. In this context strategic profitability analysis helps managers to ask the right questions: *What happens in the supply market and final products market? How customers respond to offered values? How does reduction or increase in prices affect operating profit? To what extent is profitability affected by cost management?* It is of crucial importance that the problems and their relative weights are identified as well as urgency of their resolution.

13. In a changing business environment innovations are inevitable even when products have functional and aesthetic features matching current requirements of the market. The activity of innovation is a common leverage and assumption of competitiveness because of both the activities that competitors undertake and rapid general developments in technology. From the management's and accounting perspective it is crucial that decisions made during the design (redesign) phase of the new types of output, or the related processes, predominantly affect the costs of a life cycle of product.

The accounting function should help in identifying whether investments in innovative contents are economically viable by comparing the costs and effects expected of specific type of investment, which is carried out by means of general differential cost analysis. Cost management possibilities based on target costing concept have been specifically analyzed herewith.

14. Problems and ultimate failures of banks, followed by bailout of some banks have revealed a problem of inappropriate institutional framework for banks resolution in Republika Srpska and Republika Serbia. Some weaknesses have been identified in operations of the supervisory authorities. Primarily this relates to early warning system, enforcement of timely action and finally resolution of failed banks. All cases so far have been mostly resolved or are undergoing the resolution with significant costs involved which are burden to public funds. It has become evident that supervision should be improved in terms of improving the procedures and introducing the instruments for taking the action in a bank on a timely basis. The legislation which urgently necessitates improvements is expected to introduce in the



САВЕЗ РАЧУНОВОЂА И РЕВИЗОРА РЕПУБЛИКЕ СРПСКЕ

The Association of Accountants and Auditors of Republic of Srpska

future a minimum cost approach whereby the use of public funds would be explicitly defined and subjected to clear rules.

15. The only publicly available source of information on banks includes the reports of external auditors which are being published. External audit fees are paid by banks themselves therefore some degree of “flexibility” of external auditors in expressing their assessment of whether the financial statements are presented fairly should not be excluded. The audit reports nevertheless provide to “financially knowledgeable” users a vast amount of useful information and these should be used as a basis for professional and public debate. They certainly deserve greater *ex ante* rather than *ex post* media attention as the case has been so far. Each audit report noting a financial report misstatement presents an early warning sign of a problem in the bank.

16. Republika Srpska lacks sufficient analytical procedures and the responsible institution for bank recovery and resolution. The law provides only for liquidation or insolvency proceedings and naturally for the takeover by a stronger bank. No institution has been delegated the responsibility for the recovery of a failed bank nor there is possibility to establish a “bridge” bank or to have the Central bank supporting the recovery by means of its liquidity loans. The only option remaining is nationalization or partial nationalization of the bank which provides no warranty as to success of its future operations.

17. Problems of individual, smaller banks have not caused significant problems to functioning of the financial system in Republika Srpska or Republika Serbia. In certain aspects the crises in individual, smaller banks in RS and Serbia have been helpful as in Serbia they triggered significant institutional adjustments accompanied with relevant legislative changes aimed at strengthening supervisory powers and ensuring the system for problem bank resolution. Republika Srpska has taken the same approach to legislative changes. Fortunately, neither case involved a real banking crisis rather these events served as a serious testing for crisis situations or possible systemic crises of banks. In order to ensure their undisturbed operations it will be necessary to require banks to additionally strengthen their capital base, primarily for the reason of unfavorable trend in receivables collection which leads to higher credit risk, credit losses and reduced profitability. It is of special importance that „smaller” banks strengthen their capital base as without increased bank capital they will not be able to defend their position in a turbulent banking market. In terms of the liquidity position based on the financial statements, the banking sector of the entities and Bosnia and Herzegovina is liquid and able to settle its payment obligations when due.



САВЕЗ РАЧУНОВОЂА И РЕВИЗОРА РЕПУБЛИКЕ СРПСКЕ
The Association of Accountants and Auditors of Republic of Srpska
