

FUNCTIONAL CURRENCY AND OTHER CHANGES TO THE ACCOUNTING

On November 8, 2023, a consolidation package was approved in the Senate, which, among other things, includes changes to the accounting act. The partial amendment to the accounting act mainly introduces the option of implementing a functional currency for selected accounting units, a new determination of the net turnover amount, and two other changes that only concern large companies, which will now prepare an Income Tax Report and a Sustainability Report. **The validity of this amendment will come into effect on January 1, 2024.**

Functional Currency

The amendment to the accounting act will allow accounting units to use a functional currency. This legislative change is primarily based on the International Financial Reporting Standards (IFRS). The accounting currency is understood to be the Czech currency or another currency, if it is the functional currency of the accounting unit and is either the euro, the US dollar, or the British pound. According to the definition, the functional currency is the currency of the primary economic environment in which the accounting unit operates, meaning that the accounting unit actually conducts its activities in the functional currency, rather than switching to, for example, the EUR for convenience due to its parent company, etc. Therefore, an accounting unit cannot switch to a functional currency if it is not truly the functional currency for it. Accounting units will use the exchange rate announced by the central bank relevant for the accounting currency (e.g., for the conversion of EUR, the rate of the European Central Bank will be relevant) to convert foreign currency into the accounting currency).

In the event that an accounting unit decides to use a functional currency (e.g., euro), it should be noted that the Czech currency at that point becomes a foreign currency.

Accounting units will thus need to calculate exchange rate differences, for example, when paying wages, which they will pay to their employees in Czech korunas. Although it is likely that the legislative obligation for employers to pay wages in korunas will be abolished, it will probably not be possible to pay the corresponding social security and health insurance in euros.



Accounting units that set a currency other than the Czech koruna as their accounting currency will be able to pay tax in the functional currency (e.g., in euros), but the obligation to submit tax returns in Czech korunas will still remain. Likewise, it will be necessary to keep records for the preparation of the value-added tax return in the Czech currency.

The accounting currency can only be changed on the first day of the accounting period. If accounting units decide to keep accounts in a currency other than the Czech koruna, this decision cannot be reversed. The change can only be made if another currency (euro, pound, dollar) ceases to be the functional currency.

As the approval of the consolidation package is happening close to the end of the year, accounting units have very little time to consider the use of the functional currency option (including the related setup of accounting software). Therefore, the transition to a functional currency needs to be carefully thought through and prepared for. If accounting units plan to use a functional currency, nothing prevents them from switching, for example, a year later, i.e., on January 1, 2025. The transition is voluntary at this point. We are ready to help you with the decision-making and to consult with you on the impacts for your company.

Net Turnover

Another change included in the consolidation package is the determination of net turnover. Net turnover will continue to be a criterion for determining the categorization of an accounting unit and for determining the obligation for an audit. After the amendment, net turnover will be newly determined as the amount of revenue from the sale of products and goods and from services provided during the accounting period, on which the business model of the accounting unit is based. Therefore, other operating revenues, financial revenues, etc., will not be included in the net turnover.

Along with the accounting act, there will also be an amendment to the decree for entrepreneurs, which will more specifically determine the method of calculating net turnover. In determining the includable revenues, particular attention will be paid to the sector and market in which the accounting unit operates and the nature of the accounting unit's activities. The method of calculating net turnover will likely need to be stated in the annex to the financial statements.



From the above, it is clear that it will not be sufficient to monitor turnover only on accounts of accounting class 60x, but the accounting unit will have to include all relevant revenue accounts, although a significant part should indeed be on the accounts of 60x. For easier and clearer determination of net turnover, it is highly recommended to keep these revenues on separate analytical accounts, starting from January 1, 2024.

The change in determining net turnover will have a significant impact on meeting the criteria for mandatory audit of accounting units. Since the determination of turnover after the amendment will generally lead to a reduction in net turnover (due to the inclusion of only part of the revenues), many accounting units will no longer meet the criteria for a mandatory audit. One of the criteria for an audit obligation is exceeding a net turnover of 80 million CZK.

The calculation of net turnover will be introduced prospectively, meaning that turnover already determined for past periods will not be recalculated. To assess the fulfillment of the criteria, the turnover for 2023 according to the old methodology will be compared with the turnover for 2024 according to the new one.

Income Tax Report, Sustainability Report

As part of the consolidation package, an obligation to publish an Income Tax Report (report on tax payments in other European Union countries) and a Sustainability Report will also be implemented into the law. Both of these obligations primarily concern large companies. The Income Tax Report must be prepared by an accounting unit with a turnover of more than 19 billion korunas. The Sustainability Report must be prepared by an accounting unit that is a public interest entity, is a large accounting unit, and has more than 500 employees.

Finally, we would like to mention that a new accounting act is planned from January 1, 2025, which will include many significant changes in the spirit of the International Financial Reporting Standards (IFRS), which are a major inspiration for its preparation.

We will diligently follow all the updates with the planned change to the accounting act and keep you informed in time.



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