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METHODOLOGICAL ASPECTS OF JOURNALING A DYNAMIC ADJUSTING ENTRY MODEL

V. Kašparovská, J. Gláserová

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Abstract

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This paper expands the discussion of the importance and function of adjusting entries for loan receivables. Discussion of the cyclical development of adjusting entries, their negative impact on the business cycle and potential solutions has intensified during the financial crisis. These discussions are still ongoing and continue to be relevant to members of the professional public, banking regulators and representatives of international accounting institutions. The objective of this paper is to evaluate a method of journaling dynamic adjusting entries under current accounting law. It also expresses the authors' opinions on the potential for consistently implementing basic accounting principles in journaling adjusting entries for loan receivables under a dynamic model.

accounting, expected loss, banking regulation, impairment, business cycle, specific impairments, dynamic impairments

Current status

The purpose behind using adjusting entries for loans and guarantees in banks is to capture financial losses from loan receivables and guarantees. Adjusting entries are treated in terms of their journaling and influence on bank income. In the CR, these issues to do with accounting entries are governed by the Accounting Act, No. 563/1991 Coll., as amended and supplemented for banks by MF Decree No. 501/2002 Coll., as amended. IAS/IFRS standards are binding on banks which form consolidated accounting units and issue securities, but the standards do not focus on a concrete methodology for journaling adjusting entries. IAS/IFRS standards recommend that in creating adjusting entries, the principle of anticipated losses be respected. These are defined as financial assets losses which have already taken place, regardless of whether they have been realized or not. The concrete methodology for the accounting of adjusting entries lies within the purview of national regulators. Czech accounting regulations have adopted the principle of anticipated losses as defined in the IAS/IFRS standards regarding the journaling of adjusting entries.

It has become evident during the 2007–2010 financial crisis that the strategy employed in creating adjusting entries is not in accordance with economic reality. Applying the anticipated loss principle while respecting the accounting principle of truthful representation in creating adjusting entries has led to a procyclical effect. This problem is currently under broad discussion in the profession. But no publications have appeared in the context of this discussion on methods by which countercyclical adjusting entries might be journaled.

The aim of this paper is to evaluate a method of journaling adjusting entries whose impact is countercyclical. This methodological analysis will contribute to harmonizing countercyclical economic strategy and the journaling of adjusting entries in banks.

METHODS AND MATERIALS

This paper is both theoretical and methodological in character. At its core is the evaluation of potential methodological approaches to journaling countercyclical adjusting entries. The starting point for exploring the issue at hand is an analysis of secondary data. A method of analyzing relevant

secondary data forms the theoretical framework used in the paper which enables new findings to be made for solution of the problem. These findings are used to model the journaling of countercyclical adjusting entries and their impact on the bank's balance sheet and profit/loss statement. The principal sources of this secondary data will be professional and academic articles. A further group of resources that will be used consists of legal norms: Czech law governing adjusting entries in banking, draft documents of the Basel Committee on Banking Supervision Bank for International Settlements (BIS) and European Commission documents containing proposals to modify the creation of adjusting entries by banks.

Aside from the analysis, the paper also makes use of methods founded on logical principles with pairwise linkage. These methods involve induction and deduction, abstraction and concretization used to formulate the opinions of the authors and the results of their secondary research. The method of synthesis will be used in the analysis of secondary data in the closing portion of the paper.

Existing publications on this theme focused more on the level of economics than that of accounting methodology, particular examples being Saurina (2009), Fillat and Garriga (2010), etc. Czech researchers in the area include Frait, Komárková (2010) and, marginally, Geršl, Jakubík (2010). Discussions and solutions on the topic are being discussed at the level of European and global institutions. In 2009, a joint document was issued by the International Committee on Accounting Standards Board (IASB) and the International Committee on Financial Reporting Standards Board (FASB), and the European Central Bank issued a position statement. The issue of the methodology for creating adjusting entries and their impact on the stability of financial systems is also a focus for the Basel Committee on Banking Supervision (BSBC) and the European Commission. The BSBC is working on the next version of Basel III regulatory standard for capital adequacy, which deals with adjusting entries for loan receivables. European Commission has prepared CRD II, CRD III and CRD IV (Capital Requirments Directive) to the same end.

Saurina (2009) maintains that there are two approaches to adjusting entries – an economic approach and an accounting approach. The author relates the economic approach to the economic cycle. He maintains that during boom times, banks have optimistic expectations and therefore lower loan requirements, resulting in credit expansion. The opposite obtains during periods of recession. This behavior is reinforced by an expansionary monetary policy when the aversion to risk on the part of banks is reduced as a consequence of low interest rates. The author points to contradictory development in the economic cycle, on the one hand, and, on the other, problem loans and adjusting entries related to them. In evaluating the accounting framework, the author points out that the accounting model used for journaling adjusting entries employs historical loss data for individual homogeneous groups of loans to determine the amount of adjusting entries. The author introduces the Spanish adjusting entry model, which differentiates between specific and dynamic adjusting entries. For adjusting entries in general, Saurina introduces the relationship:

$$^{1}\ dot.gen = \alpha\Delta C_t + (\beta - \frac{dot.espe_t}{C_t})C_t, \qquad (1)$$

where:

C..... is the loan balance,

ΔC ... is the change in loan balance during individual periods under observation,

α ..... covers inherent loss,

β ..... is the average value of specific adjusting entries over the long-term (the entire economic cycle).

The first component in Equation (1), $\alpha\Delta C_t$ represents specific adjusting entries and grows with increased lending by banks. The second component $(\beta - \frac{dot.espe_t}{C_t})C_t$ represents dynamic adjusting entries. Dynamic adjusting entries rise during periods of economic growth. Equation (1) shows that dynamic adjusting entries grow because specific adjusting entries during a period of economic growth are lower than the average value β. Conversely, during periods of decline, dynamic adjusting entries fall because specific adjusting entries are higher than the average for the entire cycle (β). Saurina also indicates that parameters α and β have been constructed for six homogeneous groups of financial assets:

1. cash, public sector debt (zero risk),
2. residential mortgages with LTV below 80%, companies rated A or above,
3. loans secured by real estate and residential mortgages whose LTV is above 80%,
4. other loans, including corporate and SME,
5. consumer loans,
6. credit cards.

Values for parameters α and β are defined by national regulators for these groups. The values of parameter α, depending upon the group, range between 0% and 2.5%. The values for parameter β, depending upon the individual group, range between 0% and 1.64%.

1 Although the components $dot.gen_t$ and $dot.espe_t$ are not explicitly described in the relationship, it may be deduced from the context that the $dot.gen_t$ component represents total adjusting entries and the $dot.espe_t$ component represents specific adjusting entries during the time period under examination.

The author also presents an equation to be used in determining the total value of adjusting entries which takes into account all six risk groups.

$$dot.gen_{it} = \sum \alpha_i \Delta C_{it} + \sum (\beta - \frac{dot.espe_{it}}{C_{it}}) C_{it} = \\ = \sum \alpha_i \Delta C_{it} + (\sum \beta_i C_{it} - dot.espe_{it}). \quad (2)$$

The Spanish system designates limits for total adjusting entries

Dynamic adjusting entries as a tool for reducing procyclicality are also dealt with by Fillat and Gariga (2010).

Fillat and Gariga (2010) analyze the Spanish procyclicality model as a potential methodological basis for designating dynamic adjusting entries. They present a more detailed analysis of the Spanish model than does Saurina (2009).

Their description takes as a starting point two components of adjusting entries. Specific adjusting entries serve as the basis for precise rules for each type of loan and represent anticipated loss. The second component is made up of dynamic adjusting entries, designated using a statistical model of historical losses during the entire loan cycle. The authors indicate that total adjusting entries are designated in the Spanish dynamic adjusting entries system in accordance with Equation (3):

$$GP_t = \alpha \Delta C_t + \left(\beta - \frac{SP_t}{C_t} \right) C_t, \quad (3)$$

where:

GP_t ... represents total adjusting entries,

C_t ..... is the value of the loan portfolio (the sum of loans in the bank's balance sheet),

ΔC_t ... is the change in value of the loan portfolio during a single quarter,

SP_t .... are specific adjusting entries for the accounting rules given,

α and β .... represent parameters.

Parameter α represents the long-term average anticipated loan loss in the loan portfolio, $\frac{SP_t}{C_t}$. Parameter β represents the historical long-term average of this ratio. The parameters are equal to historical averages designated using data from at least one loan cycle. The aim is to estimate the average long-term loss rate.

Equation (3) may be divided into two parts. The first portion consists of the relationship $\alpha \Delta C_t$, representing specific adjusting entries. This relationship implies that total adjusting entries GP_t grow when the C_t component grows, i.e., when loans are provided. The second part of Equation (3) consists of relationship $\left(\beta - \frac{SP_t}{C_t} \right) C_t$, representing dynamic or countercyclical adjusting entries. The relationship $\left(\beta - \frac{SP_t}{C_t} \right) C_t$ thus represents the extent to which the value of adjusting entries deviates from the long-term average during a particular phase of the loan cycle. In economic growth periods, banks have less risky loan portfolios under the influence of favorable economic conditions and optimistic expectations, the share of specific adjusting entries is lower than the long-term average and the difference is positive. During this period, the dynamic portion results in growth in total adjusting entries GP_t. During an economic downturn, the opposite is true. The difference is negative and the dynamic portion works to reduce total adjusting entries.

The authors further state that US accounting standards do not allow the creation of adjusting entries which would allow the cyclical behavior of loan losses to be compensated for. As a result, during periods of expansion, adjusting entries are not created in sufficient numbers because the level of loan losses is lower than the long-term average. They state that one approach to resolving the cyclical characteristics of loan losses is to introduce a system of dynamic adjusting entries. Later in the paper, they focus on a model for applying dynamic adjusting entries under the conditions of the American banking system.

Czech authors who have focused on the problem of dynamic adjusting entries include Frait, Komárková (2009) and, marginally, Jakubík and Geršl (2010).

Frait and Komárková (2009) note the existence of several systems for the creation of adjusting entries around the world. The authors present specific adjustments created and journaled at a time when an evident event took place which points to the likelihood of a loan loss. They designate specific adjustments as retrogressive – journaling risk ex post – created using individual receivables. At the same time, they introduce dynamic adjustments whose creation is forward-looking, created for loan portfolio losses. The authors contend that current IAS 39 regulations only allow retrogressive adjustment. The model of dynamic adjusting entries leads to actual losses normally being lower than the adjusting entries created during periods of economic growth, giving rise to a "reserve" for recessionary periods. Frait and Komárková (in the same paper) give as an example the countercyclical impact in Spain of adjusting entries. The authors demonstrate that the Czech banking sector evidences a negative correlation between GDP evolution and the development of the designated ratio indicator[2] and explore the influence of selected factors, the so-called representatives of economic

2 For a ratio indicator, the authors selected adjustments on loans for total loans.

cycle development for the development of this ratio indicator.

Geršl and Jakubík (2010) treat the problem only marginally in exploring factors which serve as the source of the procyclicality of the financial system. They argue that regulators are attempting to discover a mechanism for creating adjusting entries which would cover anticipated losses in an ideal manner within the framework of the economic cycle as a whole. In this context, they once again introduce the Spanish model as a potential solution and point to the conflict between the regulatory and accounting standpoints in the creation of adjusting entries.

The problem of countercyclical adjusting entries is also a point of focus for European and global institutions. IASB, in conjunction with FASB, created a joint consultation document in 2009 entitled *Information for Observers*[3] dealing with the creation of adjusting entries in relation to the impact of the financial crisis. This document is not officially binding. The consultation document merely points out the global significance of the problem and the necessity of its resolution.

The document is based upon a description of the creation of adjusting entries under IFRS in keeping with the IAS 39 standard. Under the IAS 39 standard, adjusting entries are based upon the concept of anticipated loss (incurred loss), journaled as a reduced value for a single asset or group of assets ("collective assessment for impairment"), based upon historical losses in this group. The *Information for Observers* consultation document labels countercyclical adjusting entries as a dynamic/statistical model, as opposed to an accounting model. The document maintains that the Spanish model does not use information about future losses but rather is a retrogressive model which makes use of historical portfolio loss data.

The Basel Committee on Banking Supervision (BSBC) and the European Commission are also concerned with methodological problems to do with the creation of adjusting entries and their impact on the stability of the financial systems. BSBC is working on a new capital adequacy version entitled Basel III[4] and the European Commission has prepared measures in this direction: CRD II, CRD III and CRD IV[5] (Capital Requirments Directive) These documents essentially deal with strengthening capital requirements and strengthening bank liquidity with the aim of reducing systemic risk. One measure for increasing the stability of banking systems proposed in the Basel III and CRD IV documents is the creation of adjusting entries throughout the economic cycle, so-called dynamic provisioning. Dynamic adjusting entries call for the creation of adjusting entries in an amount greater than anticipated losses during growth periods, with the surplus created by the adjusting entries then tapped during recessionary periods.

RESULTS AND DISCUSSION

These papers demonstrate the prevailing approach for dealing with the problem by the professional public and in the literature. The discussion focuses on adjusting entry creation models in relationship to the economic cycle.

The literature does not state how proposed changes should be journaled, even if emphasis is laid on journaling in a way which does not contradict basic accounting principles.

The aim of this paper is therefore to react to this reality and to evaluate potential methods for journaling dynamic adjusting entries in keeping with contemporary accounting principles. This proposal is put into application using accounting principles governing banks in the CR[6].

In conformance with CNB Measure No. 9/2002 Coll. and CNB Decree No. 123/2007 Coll., as amended, banks may journal the creation of adjusting entries:

- for individual receivables,
- for a portfolio of homogeneous receivables.

In either case, journaling is carried out using the same method, an embodiment of the precautionary principle in accounting as relates to the reporting of income. In accordance with MF CR Decree No. 501/2002 Coll., the gross method and indirect accounting method are used. The creation of adjusting entries is journaled as a reduction in assets with a simultaneous increase in costs. Use of adjusting entries, i.e., spending or canceling adjusting entries, is journaled as an increase in assets with a simultaneous increase in income. The impact of accounting for adjusting entries for loan receivables in the financial statement is clear from Table I. This shows valid journaling of adjusting entries and their influence on components of the financial statement in relation to the economic cycle.

Current accounting methodology respects the anticipated loss principle. Notice that in Table I,

3 See http://www.iasb.org/NR/rdonlyres/170A93CC-D8D0-4618-93D6-3F253BE238DC/0/Prov0903-joint7Cobs.pdf

4 For further details, see http://www.bis.org/bcbs/basel3.htm

5 For further details, see http://www.crd-iv.com/

6 Although most Czech banks must carry out their accounting in accordance with IAS/IFRS principles, national regulations are used in this paper, in particular the Accounting Act, No. 563/1991 Coll., as amended, and MF Decree CR No. 501/2002 Coll., as amended, since these documents deal with concrete accounting procedures for banks.

I: *Journaling adjusting entries for loans in relation to the economic cycle and its impact under current accounting regulations*

Time Period and Phase of the Economic Cycle	Time Period[x)] x	Time Period Growth Phase	Time Period Downturn
Debtor Creditworthiness	Classification of receivables into the appropriate risk category	Increase of debtor creditworthiness – classification of receivable into lower risk category	Worsening debtor payment history – classification of receivable into higher risk category
Journaling	Creation of adjusting entry	Partial spending of adjusting entry	Creation of higher adjusting entry
Balance Sheet Impact	Reduced assets and total assets	Increased assets and total assets	Reduced assets and total assets
Impact on Profit and Loss	Increased costs and reduced income	Increased revenues and income	Increased costs and reduced income

[x)] Journaling of risky receivables at their creation
Source: authors

the current system for creating adjusting entries is procyclical and deepens economic cycle phases (see the second and third periods).

Now let us see whether under the current legal context it is possible to journal the dynamic adjusting entry model given in Equations (1) and (3).

As regards the model journaling, it is necessary to accept starting assumptions which will be maintained in the journaling process:

If a loan receivable changes its risk level during the course of a cycle, it is re-categorized in a different risk category.

Loan receivables remain in the bank's loan portfolio whether or not their risk level changes.

The journaling of adjusting entries as a countercyclical impact or does not deepen the economic cycle.

Model journaling need not respect current accounting law.

Given these presumptions, there are essentially two hypothetical procedures for journaling adjusting entries with a countercyclical impact which may be proposed. These procedures are

II: *Hypothetical journaling of specific and dynamic adjusting entries in analytical records*

Time period and phase of the economic cycle	Time period[x)] x		2. Time period growth phase		3. Time period downturn	
Debtor creditworthiness	Classification of receivables into the appropriate risk category		Increase of debtor creditworthiness – classification of receivable into lower risk category		Worsening debtor payment history – classification of receivable into higher risk category	
Hypothetical accounting reaction:						
Synthetic account	Creation of adjusting entry		The total adjusting entry remains constant[7]		The total adjusting entry remains constant[8]	
Analytical accounts	Creation of a specific adjusting entry	Creation of a dynamic adjusting entry	Partial cancellation of a specific adjusting entry	Creation of a dynamic adjusting entry	Supplementary creation of a specific adjusting entry	Partial spending of a dynamic adjusting entry
Hypothetical impact on the balance sheet	Reduced assets and total assets		No impact on bank balance sheet		No impact on bank balance sheet	
Hypothetical impact on profit/ loss statement	Increased costs and reduced income		No impact on bank profit or loss		No impact on bank profit or loss	

[x)] Journaling of risky receivables at their creation
Source: authors

7 The assumption is made that the total amount of the adjusting entry remains constant, as a consequence of the fact that spending the specific adjusting entry is compensated by the creation of dynamic adjusting entries identical in amount.

8 The assumption is made that the total amount of the adjusting entry remains constant, as a consequence of the fact that spending the specific adjusting entry is compensated by the creation of dynamic adjusting entries identical in amount.

indicated in Tables II and III schematically, along with their impact on the balance sheet and income.

It is clear from Table II. that the first variant discussed involves the use of analytical records for accounting countercyclical adjusting entries. The total adjusting entry will be journaled in the synthetic account, and differentiated into specific and dynamic components in the analytical record.

The specific component corresponds to the amount of anticipated loss, with the dynamic component created at a level in excess of the expected loss on the basis of long-term average loss for the risk group in question (see Equation (3)).

It is clear from Table II. that the receivable originated during the initial period and an adjusting entry was created for it containing specific and dynamic components in the analytical record. The adjusting entry brings about a reduction in total assets and the profit/loss report shows reduced income in the amount of the total adjusting entry.

During the growth phase, the total adjusting entry remains constant, with the changes taking place in the analytical record. Assuming equal changes in the specific and dynamic components of the adjusting entries, the entry will have no influence on the financial statement.

In the declining phase, the adjusting entry total remains constant, with the changes taking place in the analytical record. Assuming equality of the specific changes and dynamic adjustments again will once again not affect items in the financial statements.

This accounting approach has a countercyclical effect. The synthetic adjusting entry in the hypothetical model does not change in relation to the economic cycle and thus is not procyclical. Changes occur only in the analytical records, where changes in the specific portion of the adjusting entry are compensated by changes in the dynamic portion of the adjusting entry.

The second model case under evaluation is making use of reserves to journal the dynamic part of an adjusting entry. This case is presented in Table III.

Table III illustrates schematically the procedure for journaling countercyclical adjusting entries by creating reserves for loan receivables. In this case, all facts are entered in the books at the level of the synthetic accounts. The specific portion of the adjusting entry is journaled using the adjusting entry and expresses the anticipated loss. The dynamic component is journaled as a reserve for loan receivables and created at an amount greater than the anticipated loss.

And adjusting entry is created at the start in the amount of the anticipated loss, as well as a reserve at an amount greater than the anticipated loss. The result is a reduction in total assets influenced by the drop in equity. There will be a reduction of income shown in the profit/loss statement amounting to the sum of the adjusting entry and reserve created.

During the growth phase, the adjusting entry will be spent and the reserve created as a result of lower anticipated losses. The result is increased total assets. The profit/loss statement will show a reduction in income dependent upon the difference between the amount of the adjusting entry and the reserve.

During periods of decline, adjusting entries are created under the influence of growth in anticipated losses and reserves are spent. There is a reduction in total assets and an increase in income in the amount of the difference between the adjusting item and reserve.

This accounting approach has a countercyclical effect. During growth periods, reserves are created in an amount higher than value of the adjusting

III: *Hypothetical account for journaling countercyclical adjusting entries with the use of reserves*

Time period and phase of the economic cycle	**1. Time period[x] x**		**2.Time period growth phase**		**3.Time period downturn**	
Debtor creditworthiness	Classification of receivables into the appropriate risk category		Increase of debtor creditworthiness – classification of receivable into lower risk category		Worsening debtor payment history – classification of receivable into higher risk category	
Hypothetical journaling	Creation of adjusting entry	Creation of reserves	Partial cancellation of a specific adjusting entry	Creation of reserves	Creation of adjusting entry	Cash expenditures
Hypothetical impact on the balance sheet[xx]	Total assets are reduced		Total assets rise		Total assets are reduced	
Hypothetical impact on profit/ loss Statement	Reduction in income due to higher costs		Reduction of income by the amount of the difference between adjusting entries and reserves		Increase in income by the amount of the difference between adjusting entries and reserves	

[x] Journaling of risky receivables at their creation

[xx] The assumption is adopted that the reserve is created at a constant amount and of greater value than the adjusting entry as an anticipated loss

Source: authors

entry spent. During periods of decline, reserves are spent in an amount higher than the adjusting entry created.

The hypothetical system noted above for journaling countercyclical adjusting entries in keeping with assumptions 1–4 does not fulfill some accounting principles. The economic basis of countercyclical adjusting entries thus conflicts with journaling possibilities which respect current accounting principles.

Both proposals (Tables II and III) conflict with the current principle of anticipated loss as the economic basis for creating adjusting entries for loan receivables. Given that the anticipated loss is understood as an existing loss, the dynamic portion of the adjusting entry cannot represent the anticipated loss, since this portion is created as a "reserve cushion" for the future decline in the economic cycle. In terms of economics, then, the dynamic adjusting entry in the analytical records in Table II and the reserve created in Table III do not have the character of anticipated losses.

The hypothetical procedure for journaling countercyclical adjusting entries simultaneously preaches the accounting principle of accurately representing the facts, since the adjusting entry, or the dynamic component of the entry, is created even if there is no increased loan risk.

It is further clear that the hypothetical journaling in Table III, carried out in accordance with presumptions 1–4, conflicts with the accounting principle which forbids the simultaneous creation of a reserve and adjusting entry for a single receivable.

Let us focus now on resolving the conflict between the journaling of adjusting entries for loan receivables and the economic basis of countercyclical adjusting entries as described under the Spanish model.

Were regulators to adopt a framework for countercyclical adjusting entries, one solution would be modification of existing accounting principles. The primary import would be to change the conceptualization and content of the expected loss. This is a complex problem whose solution is tied not only to changing the content of expected losses in creating adjusting entries itself, but also in changing the conceptualization of unanticipated losses as far as the capital requirements of banks goes. In this case, collaboration is required between those creating accounting regulations and bank regulators creating proposals dealing with bank capital requirements.

Another solution would be to make it possible to practically implement journaling of countercyclical adjusting entries with the conquering creation of adjusting entries and reserves for receivables (see the model in Table III). In this case, the creation of reserves would represent a cost connected with the creation of the "cushion" to cover losses during the recessionary period and the development of reserves thus created would react to macroeconomic indicators. As regards the impact on the development of taxable net profit in the bank, it would be necessary to create limits for the creation of reserves as taxable costs.

Because of the countercyclical nature of adjusting entries, Niedermayer *et al.* (2010) say that dynamic adjustments will lead to temporary or permanent reduction in bank profitability. This statement is open to question, because the hypothetical models given in Table II and Table III indicate that if analytical records are used along with reserves for journaling adjusting entries, no pressure will be created ceteris paribus for increasing total costs for loan receivables long-term or throughout the economic cycle. The reason for this is that the creation of dynamic adjusting entries or reserves entered into costs during the growth phase will be used during the recessionary phase and will thus be accounted as revenues. It is not methodologically correct to monitor the impact on costs over a short-term timeframe which represents only a portion of the economic cycle. This will lead to distortion of the effect being reflected in the bank's income over the long-term. The impact of countercyclical adjusting entries on costs and bank income must be evaluated at a minimum for a period of one entire economic cycle.

In summary, modifications which are necessary to fulfill the requirements of journaling countercyclical adjusting entries will be the result of agreements and compromises between banking regulators and representatives of international accounting institutions. At the same time procedural steps must be defined for transitioning to a new method of creating and journaling adjusting entries. The procedures and their impact must be empirically verified throughout the economic cycle.

SUMMARY

This paper expands the discussion of the importance and function of adjusting entries for loan receivables. Discussion of the cyclical development of adjusting entries and potential solutions have been under intense discussion during the period of financial crisis continue to be relevant to bank regulators and representatives of international accounting institutions. The aim of this paper has been to describe and evaluate possibilities for journaling countercyclical adjusting entries within the framework of current accounting regulations and to express an opinion on journaling countercyclical adjusting entries. The theoretical springboard for the paper is a description of the Spanish model of countercyclical adjusting entries, which has been empirically verified. Using the parameters

given in the Spanish model results in the formulation of two hypothetical models for approaches to journaling countercyclical adjusting entries based upon predetermined assumptions. In spite of the fact that both models attained a countercyclical effect in the creation and use of adjusting entries while respecting the assumptions adopted, some accounting principles were not complied with in the process. It may just be plainly stated that the effect of countercyclical adjusting entries and their journaling will be possible only with the revision of some accounting principles. One possible solution is to alter the conception of anticipated loss which currently which currently forms the basis for journaling adjusting entries for loan receivables. The final form of these modifications, if they are to occur, will be the result of negotiations and compromise between banking regulators and international accounting institutions.

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Address

doc. Ing. Vlasta Kašparovská, Ph.D., Ústav financí, Ing. Jana Glaserová, Dr., Ústav účetnictví a daní, Mendelova univerzita v Brně, Zemědělská 1, 613 00 Brno, Česká republika, e-mail: kasparov@mendelu.cz, jana.glaserova@gmail.com