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# INTERNATIONAL JOURNAL OF ENTREPRENEURIAL KNOWLEDGE

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## CONTENTS

<b>Editorial</b> .....	4
<b>Research</b>	
<b>Tereza Benešová:</b> Towards Entrepreneurship: Reflections Between Theory And Practice .....	5
<b>Jaroslav Belás, Michal Korauš, Lenka Gabčová:</b> Electronic Banking, Its Use And Safety. Are There Differences In The Access Of Bank Customers By Gender, Education And Age? .....	16
<b>Přemysl Bartoš, Aleksandr Ključnikov, Boris Popesko, Jiří Macháček:</b> Are Men More Innovative And Aggressive In Business? Case Study From The Czech Republic.....	29
<b>Sorana Mihaela Manoiu, Maria Ionela Damian, Jiří Strouhal:</b> Corporate Governance Quality On Specific Case Of Romanian Listed Companies.....	40
<b>Karel Slinták:</b> Cultural Reversal: Why Does Obedience Lose With The Initiative.....	59
<b>Kristýna Havlová:</b> IFRS Versus CZ GAAP: Influence Of Construction Contracts On Financial Indicators.....	76

## Editorial

Dear readers and colleagues,

It's been two years since December 2013, when the first issue of our journal was published. The Journal of Entrepreneurial Knowledge is now entering the third year of its existence, and it looks to be the right time for a small reflection on what we managed to achieve. Without excessive modesty we can state that the journal has got into the subconscious of the professional public, as evidenced by the interest of the authors to publish their contributions in IJEK, but also the inclusion of the journal in the "ERIH +" database. Our aim is to keep the standard of publishing of the entrepreneurially related high quality scientific articles written by recognized experts and get IJEK listed in Scopus database in the nearest future.

As is evident from the name of the journal, the purpose of its existence is to create a platform for the publishing of entrepreneurial knowledge. And it is not a simple assignment - it requires the connection of theoretical knowledge with practice, hunting for the ways of seeking new opportunities for business, but also for the forms of its implementation with regard to business related risks. To fulfill this purpose we would like to create several sub-platforms that will promote the different business related categories in the journal. We will continually work on the development of these platforms by creating the specialized chapters for the appropriate individual contributions.

It will thus create the space for the analysis of business opportunities, risk management, enterprise economics and finance, new methods of marketing and management, the use of information technology in business, business in the non-manufacturing sector and non-traditional areas. Negligible role for the business sector is played by the knowledge of the legal forms of enterprises and related obligations, including the prediction of possible impacts of non-compliance with the obligations (commercial judiciary, the effects of the measures the EU or WTO).

It is therefore evident that our journal can cover the wide scope of entrepreneurial topics and provides the space for the presentation of new findings in the field of business and all the consequent activities. Let us, therefore, to the next year of our joint activities of many imaginative and original contributions that will benefit everyone, both readers and writers.

We wish to attract many imaginative and original contributions that will be helpful for both our readers and authors in the next year 2016.

Your Editorial Board



## TOWARDS ENTREPRENEURSHIP: REFLECTIONS BETWEEN THEORY AND PRACTICE

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### ABSTRACT:

*The paper deals with the pragmatic need of linking theory and practice in the learning process, focusing on vocational education in economics and entrepreneurship education. In connection with selected alternative economic theories is shown the necessity of praxeological educational background and practical work experience in teaching process in entrepreneurship education. Results are based on the research, which was done in the framework of prepared dissertation thesis on the theme of entrepreneurship education from the perspectives of theory and the perspective of vocational school teachers of economics subjects. The results focus on the concept of entrepreneurship education preferred by teachers of the economical subjects at the secondary schools specialised in economics. The main aim of the research was to check, to what degree are the theoretical bases of the education of the entrepreneurship fulfilled in the reality of a secondary school specialised in economics. The results show that in the case of preferred aims of the respondents of our examination we could talk about the combination of creation of knowledge and preparation for the profession. It is confirmed that the teachers rely significantly on a prescribed list of educational topics, but at the same time the results clearly show that the respondents think about their subject and formative aspect of their classes through using of cross-sectional topic.*

### KEY WORDS

*entrepreneurship education, late modernity, reflexivity, facilitation*

### JEL CLASSIFICATION

A22

### 1 DECISION MAKING UNDER UNCERTAINTY AND RISK

The postulate of uncertainty as an integral part of our (not only) economic life, as was formulated by John Maynard Keynes more than seventy years ago (Keynes, 1936), and rejection of prognostic pride of economics of the mainstream is now, in the wake of economic crisis, viewed as a necessary condition for understanding human behaviour.

Uncertainty in the ontic sense of a Post-Keynesian explanation<sup>1</sup> is viewed as an inherent feature of the world, which does not prescribe, what will happen, but what can happen (Shackle, 1969). This uncertainty comes from human action, which is irreversible and changes circumstances and conditions so that they cannot be repeated in the absolute meaning of the word. The human ability to make decisions and to influence not only surrounding conditions, but also the human, however, does not correspond to the image of mechanical calculation, as is favourably used in economics, as a mathematically-allocated science<sup>2</sup>.

A decision is in this sense a creative act the result of which is not defined by natural necessity, but is in its own way a *self-destructive experiment* (Shackle, 1969; Svoboda, 2002). This means that every piece of knowledge we obtain causes qualitative change inside of us. This approach corresponds to the basis of the conceptions of procedural rationality or theory of limited rationality and critics of neoclassical economics<sup>3</sup>, create many implications (not only) for professional economics education.

The flow of Post-Keynesianism does not forget the fact that human knowledge is fallible in that it is a social product, reminding us of how (not only economic) subjects view uncertainty; it is given not only by personal values, cultural and social patterns, but also by (not only economics) theories influencing them (Svoboda, 2002). That involves questions of theoretical *concepts* and their influence on thinking and acting.

We will limit ourselves, in this article, on the consideration of the character of *knowledge*, which is based on a realisation of the changing of the outer and inner worlds, and the way it accepted.

### 1. 1 Second age of modernity

The acceptance of uncertainty comes together with a theses of the second age of modernity (Beck, 2004, 2006; Keller, 2007), or late modernity (Giddens, 2003; Chisholm, 2008; Navrátil, 2009). The impeachment of a scientific way of knowing and the validity of theories which we wrote about in relation with Post-Keynesianism comes through the social sciences. Searching for one objective truth is subsidized by a sensitive and critical evaluation of rival explanations (Navrátil, 2009). The important consequences of late modernity are concepts of personal and theoretical reflexivity (Beck, 2004, Giddens, 2003; Lynch, 2000; Navrátil, 2009). Reflexivity in the meaning of the deconstruction of objective knowledge, revaluating the way of thinking about things, especially in connection to critical theoretical reflection and the *reflexive (my)self* (Giddens, 1991) is an important impulse for our debate.

The present *society of knowledge* or society of understanding, that is society with a decisive role of human capital and the externalisation of creative functions, is characterised by the growing pressure of demands on high and constantly innovative knowledge, the need for creating unique technologies, products and systems, reflectively made knowledge and other features from the

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<sup>1</sup> Post Keynesian economics is one of approaches, which representatives complement and reinterpret Keynesian theory. It attempts to supplement Keynesian theory of effective demand, not only with imperfectly working markets, but also with alternative theories of dividing, value and money, which could allow to form from Keynesian theory adequate alternative to neoclassical economics.

<sup>2</sup> For example, Tomáš Sedláček (2009) points out the problems of present economics science, which is excessive shift to mathematisation of economics theory.

<sup>3</sup> These are post-classical approaches, which affect argumentation routine of paradigm *homo oeconomicus* (Hlaváček, 1999).

collateral phenomenon of present society, for which there is in many studies and analyses the term *era of symbolic analytics*<sup>4</sup> coined by American economist and sociologist Robert Reich (1995).

The authors from the Institute for Research and Development of Education Institute of the Faculty of Education of Charles University (Černý & Greger, 2007) warn about growing demand for *knowledge workers* and about a gradual change of professional structure and job market that is in need of higher qualification and with this related higher participation on formal and informal education. The reflections of this demand are then gradual changes in social stratification<sup>5</sup> that is also the danger of disconnection of elite of society of knowledge from the rest of the population.

Generally speaking we can say that the economic-social changes in recent years have to be reflected in the processes of drafting of curriculum<sup>6</sup>, if we take into the account that the curriculum is not understood as a changeless construct, but as a dynamic process, which evolves and changes and is influenced by different types of situations (Beran, Mareš & Ježek, 2007).

On the other hand, the revision of demands put on the education for the society of knowledge cannot lead only to escalation of new and new topics, or to a non-conceptual matching of content of education to the most actual economic-social situation.

All efforts for a progressive curriculum, so called *curriculum of future* (Černý & Greger, 2007), cannot be realized without a balanced approach between the will to react on the actual needs of the society, the job market and awareness of *anthropological dimension of education*, which deals especially with cultivation of a personality of a young person, enriching his or her inner experiences, be it from the understanding, or from the experiencing of the subject matter, or interpersonal relations, which the school and its education offer. Here belong the creation of a basic value orientation, the knowledge of one's place in the system, the knowledge of relation of one to another. How a person decides, which of these influences lead him or her through life, what plans does one have and where does one head (Skalková, 2007).

With a reference to the period of the late modernity and its changeability, we cannot omit tendencies to wipe borders between education and work. The approach based on the competencies is often connected to the job market, employability and to the ability of a person to actively and without problems deal with complex, quickly changing tasks<sup>7</sup> (Janík 2005; Janík et al., 2010; Janík & Slavík, 2011). Factual knowledge and routine skills are becoming less and less sufficient and adequate skill set of a person (Chisholm, 2008). New topics are put into the curriculum of the present school and there are new demands. Solutions of problems, the analytical critical thinking, the reflexive way of creation of knowledge, the ability of self-directing and other required *skills for*

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<sup>4</sup> The symbolic analyst (sometimes not exactly identified with known expression from Peter Drucker „knowledge worker“) is in a concept of Reich and following authors ideal representative of society of knowledge. The symbolic analyst is highly professionalised, competent, and globally mobile. Among key skills of symbolic analysts belong ability of abstraction (work with models, formulas, and analogies), system thinking (connection of notes from different areas), and ability to experiment and learn on the base of experience (reflectively formed knowledge), creativity and teamwork.

<sup>5</sup> We speak about a social analogical stratification with division of the job market into three segments, where upper 20% is formed by highly professionalised people, on the opposite lower 20% are unemployed people, not able to revise and complement their knowledge. Broadest segment covers 60% of able to work persons, who are, however, very vulnerable to quick changes of qualification (for example Černý, Greger, 2007)

<sup>6</sup> The curriculum is understood here in a broader meaning of this term. As an content of all experience, which students get at school and from activities connected to school, its planning and evaluation (Průcha, Walterová, Mareš, 2008).

<sup>7</sup>The goal of the article is not to be concerned deeply by the critical discussion about the term - key competencies. The use of this term has its source mainly in the concept of competency, how it is suggested by Janík, Maňák, Knecht (Janík and collective 2010)

*new jobs*<sup>8</sup> return attention to the formative task of education and the interdisciplinarity not only in the sense of the connection of knowledge from different subjects, but also in the meaning of the connection of education in an area of taught subjects with the learning in other contexts (for example at workplace), leading to a desired innovative reconfiguration of knowledge.

### 1.2 Professional knowledge: knowledge on the edge of learning and work

If we shift the attention to the area of professional education<sup>9</sup>, in relation with succinctly formulated professional profiles of graduates<sup>10</sup>, competency approach is offered (in the meaning of getting the qualification for a certain activity) as completely natural. Is it really so and is it enough? Chisholm (2008) in the relation with displays of late modernity warns that present society works in a larger scale without any borders and limitations. This means that personal, social and professional paths are more and more differentiated and individualized. He shows as an example the hierarchy of educational motives, needs and preferences:

Individuals are not divided into separated drawers with signs “general education” and “specialised education”. In the real life these categories overlay one another and this pragmatic interconnection is evident in everyday use of knowledge and competencies (Chisholm in Novotný Eds., 2008, page. 63, translated from Czech by author 2014)

Obtaining of specialisation in the meaning of getting a qualification for job, supported by the inductive *construction of knowledge* (Janík, 2005), at best in an active experience of practical action, is viewed as optimal from the point of view of demands of dynamic present.

Chisholm (2008) further expresses persuasion that individuals who actively learn themselves, reflexively, decide about what can be understood as knowledge, which knowledge belongs to one another and how it can be used. If the learning subject is so self-interpretative and builds primarily on the reflection of his or her own experience, what relation to the practical knowledge, is the knowledge gained by science and research<sup>11</sup>?

The basis for the consideration about the character of this relation is an example of training for enterprise in specialised education of economics.

## 2 QUESTIONS ABOUT THE EDUCATION OF ENTREPRENEURSHIP AND ENTERPRISE

In accordance with a competency approach, we come across with prescriptive demand in specialised economics education, but we also realistically see the need of development of *competency for initiative and enterprise skills*.

A common denominator in terms of enterprise competency, development of spirit of enterprise, a competency for enterprise, a sense for initiative and enterprise (which cannot be seen as pure

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<sup>8</sup> New Skills for New Jobs is a common social political initiative of European commission from states of EU. See: European Commission (2009): *New Skills for New Jobs: Anticipating and matching labour market and skills*. Luxembourg: Office for Official Publications of the European Communities.

<sup>9</sup> Specialised education (vocational education) covers a vocational preparation work of non-university type. (Průcha, Mareš & Walterová, 2008)

<sup>10</sup> General educational programmes (NUOV, 2007).

<sup>11</sup> More about the category of knowledge see In Janík, 2005.



synonym<sup>12</sup>), is the acceleration of the human potential, be it in social-economic development or in a more intimate level of personal development, including personalisation of values and approaches, such as a sense for initiative, independence, readiness for innovations in personal and social life and at work.

A politically-social context of the concept of the key competencies and requirements set on the education in area of competences in European Union at the same time put *enterprise* into the position of main categories of school education.

The hallmark of actuality is given by the possible trends of evolution of education and work towards actuality of requirement of cultivation of enterprise through the education and the training, in a larger context of social changes, as they are presented by all kinds of prognoses and scripts for the future with the forecast of higher work fluctuation, mobility, a need of self-employment, creativity, critical thinking etc.

The question how we should approach the problematic of support of the enterprise in the training and educational process comes after the question why we should concentrate on the enterprise. The teachers are the main agents in the reality of educational process – they change approach towards new topics in education and provide needed competencies.

According to Gibb (2007), acceptance of an appropriate and modern concept of development of enterprise and education of entrepreneurship needs among others:

- a larger integration of knowledge (in scheme of educational institution, among different branches, among art sections and science, among tacit and explicit knowledge);
- a larger interdisciplinarity of education;
- more opportunities for experience learning;
- a larger area for validation of explicit knowledge in practice (more time for reflection and learning of activities themselves);
- larger balance in emphasis on **what** is taught and **how** it is taught;
- an innovation in evaluation of programmes and accreditations;
- changes in some basics of philosophy of education.

## 2.1 Content of education of entrepreneurship

Johannisson (1991, according to Fayolle, Gailly & Lassas-Clerc, 2006) distinguishes five levels of content of development of entrepreneurial behaviour: know-why (approaches, values, motivations), know-how (skills), know-who (short and long term social skills), know-when (intuition) and know-what (knowledge). Johannisson (ibid) warns that traditional education of enterprise contains too much mostly declarative knowledge about partial processes during setting up of a business and running of a company, and that most programmes of economic education, which concentrate on enterprise are unilaterally aimed (Gibb 2007, Kirby, 2002). But content of such education of enterprise does not correspond to activities, which entrepreneurs do after starting of their business in reality (Gibb, 2007; Malach, 2008) and it does not reflect alternative theories of economics, which are close to the realistic enterprise process in concept of procedural rationality and which in

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<sup>12</sup> The English terminology, which works with the term of entrepreneurship education (common in European curricular documents), usually does not differentiate between the terms training and education, it is not only about teaching entrepreneurship, but also about entrepreneurial education (meant as education for a job – education of the future entrepreneur), and also about the training for enterprise (cultivation and development of certain specific quality – entrepreneurship).

opposite of theory of the mainstream does not abstract from imperfections in process of economic decision making and takes into account *enframing* of the process.

It is possible to state that the education of entrepreneurship is not often accepted in broader concept as a development of behaviour of enterprise and does not take into the account the fact that it can come to an enterprise acting in all kinds of environments that the enterprising behaviour is framed by a context of surrounding world, personal qualities and motivation.

A theoretical answer for this imperfection in training for enterprising can be concept of *effectuation*<sup>13</sup>, which in the present represents an influential approach to research, how entrepreneurs act, think and what do they do. Main points of this theory can be summed up like this (Sarasvathy, 2008):

Experienced entrepreneurs:

- base on the knowledge who they are, what they can do and who do they know;
- immediately act and enter interactions with other people;
- concentrate on what they can do, without large worries about what they should do;
- share some of the interactions and acting, give and bring commitments, which they can contribute to a given purpose;
- know that each commitment leads to new instruments and new goals;
- gradually gather sources that lead to clarifying of aims, decreasing of possibilities of change and creation of network of interested people;
- make goals and network gradually come closer together into new market and new companies.

This approach convenes with the theses of procedural rationality: an individual is constantly forced to confront his conceptions; equipment of perceptive and behavioural habits and to evaluate his possibilities with a changing reality and at the same time is equipped with the ability of adaptation and learning. Personal flexibility, awareness of insecurity and instability define to a certain rate the quality of one's life. At the same time with regards to the environment of a fundamental insecurity, a person is never able to objectively maximize benefit, as it is presumed by neoclassical economics. In the end, defining are not our goals, but our actions.

An example of a procedural rationality in an economical thinking, not to say a concept of effectuation represented by research activities of Society for Effectual Action, introduces suitable theoretical bases for an effective training for enterprise. Normatively oriented images, classic managing economics (especially in a relation to process of enterprise) cannot reflect reality; it abstracts from a changeable base of a relation of an individual self and the environment. The concept of dynamically influencing forces, as it is brought up for example by Saravathy (2005, 2008), takes advantage from the reflection of experience, it has *praxeological* character.

The main agents of changes during education in approach to new topics in education and intercession of needed competences are the teachers.

An emphasis on ability of synthesis of notes, on discovering, implementation of students into practical activities, orientation on creation of new ideas, opening of original views, which is essential for support of enterprise thinking and enterprise abilities goes hand in hand with an basic functional choice of the content of education goes hand in hand the

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<sup>13</sup> Author of the concept of effectuation is professor Saras D.Sarasvathy, who under the influence of Herbert Simon and his theory of procedural rationality (bounded rationality) and researches among expert entrepreneurs, supports concept of enterprise as a dynamic and highly interactive process.

Research platform for development of concept of effectuation is Society for Effectual Action.

<http://www.effectuation.org/>

A defining and necessary factor of enterprise education and training is also a stimulating environment, sharing of experiences and suitable didactic tools, among which can be labelled as most effective those, which support learning “through life and experience”, this means through practice (coaching, mentoring and facilitation), stimulation, experiments, creative problem solving, discussions, role playing and last but not least reflection of models and outer world.

Králová (2007) defines the areas of desirable change in secondary education of specialised economics as follows:

- a setting of general knowledge basics;
- an adjustment of specialised content to evolution of new technologies;
- organisation of work.

Based on these demands, the attention of the teachers of specialised economics subjects concentrates especially on the area of organisation of work in education (VŠE, 2007). Support of creative force of an individual, one’s self-reflection and an interaction with environment, emerges especially during considerations about suitable didactical techniques, teaching methods and organisational forms of teaching. There is a risk of purposelessness in the creation of these innovative educational processes without the link to the theory and the consequences with the content of education.

If we look under cover of activities and processes in present most known and spread projects supporting enterprise in education (student companies, fictional companies, Simgames, business games and so on)<sup>14</sup> we get the common denominator: learning through simulation in the safe scheme of a fictional world how to react to challenges of the real world. In newly tried roles (work relegation, work duties and responsibility) students keep their own personal characteristics and enter the process of decision making in model situations, problem solving and at the same time they realise their personal and social awareness.

We are getting beyond the borders of “simple” interactive game, which models professional or life situations, which is understood as an opportunity to try one’s abilities in an area, where he or she does not risk anything (Petty, 2008). In context of the cognitive behavioural theory it is especially about the development of ability to know, and how to organize what we know according to certain aspects, to distinguish mutual connections, to anticipate, detect mistakes in own cognitive process and to know how to dispose them by the use of the reflexive approach; that means a way to a new style of thinking and behaving.

The core of efficiency of simulation games or role playing in the meaning of a certain complex learning activity, where students in many roles get to know a simplified model of reality (Pasch, 1998) is not based “only” on getting new skills, but also on the facilitation of the inner process of change. The modelling and rehearsing of roles and skills goes together with the realisation of functional and not functional behaviour, approaches and further self-reflection.

The teacher in such education does not fill only the role of a specialist (theoretical knowledge of topic, but also field didactics), but he also fills the role of a reflective practitioner (reflexion of own experience, naming of process and a concept knowledge) and also a role of a sensitive facilitator (accessing and providing of desired values and attitudes).

### **3 TEACHER OF VOCATIONAL ECONOMICAL SUBJECTS IN CHANGES OF ROLES**

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<sup>14</sup> Detailed information at: [www.simgame.org](http://www.simgame.org), [www.nuov.cz/index.php?page=cefif](http://www.nuov.cz/index.php?page=cefif), [www.jacr.cz](http://www.jacr.cz), [www.businessgames.cz](http://www.businessgames.cz)

„In the present situation majority of teachers has not gone through a specialised training for teaching of entrepreneurship. They may not realise the correct approach to the education. The teachers should better understand the entrepreneurship education and its aims, methods and content. It is necessary to provide more specialised preparation, seminars and workshops and spread understanding of different ways and methods for support of entrepreneurial thinking.” (European Commission, 2009, page 24, translated from Czech)

The knowledge of field, the skills and the experiences of teachers are, of course, the pillar on which it is possible to build a meaningful construct of an entrepreneurial education. It is necessary to emphasize the premise that “the entrepreneurial education should not be changed with general business, or commercial studies, because its main aim is to support creativity, innovation and self-employed people for consideration about needed components of teaching and training for enterprise and entrepreneurship” (European Commission, 2009, translated from Czech).

This premise corresponds with the statement of American philosopher and founder of modern management, Peter Drucker that from the point of view of the job market, the preparatory education on universities has to prepare students much more for all life employment than for a particular job (Drucker, 2004).

Besides knowledge “about entrepreneurship” it is necessary to emphasize not only the connection of theoretical notes with practical skills, but also their practical “validation”, testing in reality, or experimenting.

Specific, supporting, didactical tools created for the support of the education of entrepreneurship, or the training for the enterprise, cannot fill their purpose by themselves and lead to the given goals without a good guide and a facilitator of process of learning. The teacher is in the position of organiser, motivational agent, and supplier of feedback, be it in the demanding process of leading of fictional company, or “only” in analysis of case study. This means that teacher suggests and leads more, than just gives orders. He learns together with the students, he works as a diagnostician, helps to solve discords and hardships, which can arise, inspires and guarantees safe environment.

The success of a supportive process depends not only on the whole set of communicational skills, such as active listening, ability to negotiate and work in teams etc., but it also depends on a sensitive bonding of oneself with the group, in an awareness of ones integrity, an ability to become a mirror of collective work and an ability share collective experience of learning.

A very fragile balance should be kept by the teacher also in the question of goal, which should be reached by the group work. The facilitator should know and monitor his goal, and at the same time respect possible borders and limits, or on the other hand talents of members of his group. This means not only the teacher’s own self-reflection, but also knowledge of abilities, imaginations and aspirations of those who he leads – only this is how it is possible to choose a forceful way of leading and to harmonize the creativity of all involved.

It is not possible to presume that each teacher (present and future) is equipped with the ideal amount of intuition, emotional intelligence and belief which makes the process of facilitation natural for him. Usually a part of this process is a certain amount of inner or outer resistance. Anti-resistant strategies then unwind in intentions of successful or practical intelligence theories and their characteristics: an ability to learn from experience, openness to change, interpersonal skills and more and more required ability of self-reflection and reflection of practical (Lazarová, 2005).

The term reflexivity in pedagogical practice emerges from its broad semantic field especially in the meaning of looking back and evaluation of acting. Looking back should be implemented into the

future actions. So the required reflection will not be only a reproduction, but will be somehow an epoche, over stepping everyday reality is needed, it is necessary to open to the reflection connected to the ability of realising of contexts and the relativity of reflected knowledge, its dependence on perspective of the person involved, which is created by a volume of knowledge and personal components, components of values, or approach.

In balance with the theory of constructivism it can be noted that there is not reality “by itself” that it does not make sense to speak about it, without being aware of an constitutive process, which is based on the mutual acting between knowing and known.

The teacher in the position of the reflective practitioner (Janík & Slavík, 2011) and the facilitator in the process of the training for the enterprise should realise himself that even public discoursus about the entrepreneurship (or the enterprise) is not homogeneous and there are many statements said from different positions, with different motives. During the analysis of the discoursus it is necessary to respect its diversification and to respect contexts in which are said partial opinions. The teacher can be the creator of own coherent argumentation, which is an integrating element of process of teaching (learning) only based on such sensitive, reflective acting.

The theory helped us to map the concepts of entrepreneurship and the theoretical approaches towards the development of the entrepreneurship and helped us to identify three topical areas, which form a complementary whole of the education of the entrepreneurship, and which can be related to the theory of an accented holistic view of the entrepreneurship based on three pillars: the personality of the entrepreneur – the social context of the entrepreneurship – the entrepreneurship as the process of the growth. We monitored three main topical areas (personal, social and work), in the scheme of the education of the entrepreneurship, which is related to a theoretical basis.

The teacher and the teacher’s thinking about the pedagogical reality and its intentionality, directivity are the key conditions for an efficient education of the entrepreneurship. The effective education of the entrepreneurship consists also, as we pointed out, of important determinants, such as the context of the culture of the school, the community and outer environment, where the theoretical notes brought a request for a guidance of the education of the entrepreneurship through enterprise, be it real or just practice and the request for a tight connection to the real world of the enterprise.

The main aim of our research was to check, to what degree are the theoretical bases of the education of the entrepreneurship fulfilled in the reality of a secondary school specialised in economics. The chosen basic perspective for the checking was the point of view of the teachers of economical subjects and their concept of the aim of the education. The main research question focused on the concept of the aim of the education of the entrepreneurship by the teachers of the economical subjects at the secondary school specialised in economics.

Partial questions were connected to the main research question. These questions were related to other chosen determinants of the education of the entrepreneurship which are identified in the theoretical part of the thesis. In the relation to the fact that the respondents inclined more to the aim category of knowledge, we can see them generally as a type of a person who concentrates on the education and training. These persons concentrate on the educational questions more in general, than on the level of the individual student and this person relies on the knowledge of the field.

334 respondents of online questionnaire in our research – the teachers as the whole, significantly inclined to the choice of the educational aims in the area of the knowledge and in the topic area of work and employment. The results show clearly that in the case of the preferred aims of the respondents of our examination, we could talk about the combination of the creation of the knowledge and the preparation for the profession. It is confirmed that the teachers rely significantly on a prescribed list of educational topics in the school curriculum, but at the same time the results



clearly show that the respondents majorly apply a cross-sectional topics in their classes. This means that they also think about their above subject and formative aspect of their classes, what corresponds with the holistic trends of entrepreneurship education.

#### 4 CONCLUSION

The late modernism is with its perception of a person as a social being with limited rationality, moving in a world of uncertainty, finds its reflection in social sciences including economics. The originality of individual life paths, project of reflective me and an essential relation of the social life creates a scheme for consideration, what declarative, procedural knowledge, and what attitudes and experiences should be goals in the education of specialised economical subjects.

An agreement is in a harmony with a competency model in preparation for a certain personal alertness, preparation for performance, a decreasing of space between learning and practical reality. In the connection to the training for the enterprise there are possible some specific didactic tools based especially on the simulation of real activities in the enterprise. The real learning through practice requires, besides providing opportunity for acting, also providing of opportunities for self-reflection and for reflection of a theory.

If practice should lead to restructuring of the theoretical knowledge and its relation to own skills, abilities and approaches, as to the environment and other outer subjects, in a way it is demanded by the modern conceptions of the education of the enterprise and the training for the enterprise, it is necessary to count with a support of the reflexive process behind theory and practice.

This support can be provided in the educational process by the teacher with facilitation equipment, who admits that fundamental insecurity influences decisive processes not only in the process of the enterprise, who admits the plurality of individual and social bases and the need to reflectively consider how to connect theoretical contents with practical action.

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## **ELECTRONIC BANKING, ITS USE AND SAFETY. ARE THERE DIFFERENCES IN THE ACCESS OF BANK CUSTOMERS BY GENDER, EDUCATION AND AGE?**

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### **ABSTRACT**

*Electronic banking is an important area of banking activities, under which the commercial banks try to retain existing clients or attract new customers through a better quality of service and decrease in prices of these services. The aim of the article was to examine selected attributes of security and the use of electronic banking and quantify differences in approach of the bank customers by gender, education and age. Our research confirmed that the dominant part of banking customers use electronic access when managing their personal finances. We found out that there are some differences in the approach of the bank customers in terms of their education. The customers with higher education to a greater extent and more intensively use electronic banking. In the safety area, we did not find any significant differences between banking clients by gender, education and age. The only exception is the finding that clients up to 35 years are significantly more confident in the use of electronic banking through public networks.*

### **KEY WORDS**

*Commercial banks, electronic banking, the use of electronic banking, electronic banking security, gender, education, age*

### **JEL CLASSIFICATION**

*G21*

### **INTRODUCTION**

The rapid development of information and communication technologies in recent years has triggered a wave of innovation in the banking sector and led to the emergence of new distribution channels, electronic banking (e-banking), and it represents extensive opportunities in the way of organizing of development of financial products for the bank, as well as the distribution of these products to clients through the Internet. Better technology, more distribution channels and greater

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flexibility brings more significant effects in terms of quality of banking products and ultimately it means a higher degree of satisfaction of customer needs (Sysáková and Šlahor, 2010).

Electronic banking is the most advanced and most dynamically developing *direct form of communication* between the bank and the client in the form of electronic connection where the client does not come into personal contact with employees of the bank. It uses communication media such as a personal computer with a modem, telephone, mobile phone, etc., so it carries out operations from its terminal or other publicly available technical equipment (Tkáčová et al., 2009).

The use of these new distribution channels highlighted the important role of banking security, because the environment is more vulnerable to system attacks (Koskosas, 2011; Dhillon and Torkzadeh, 2006). According to Fatima (2011) delivering of financial services over public networks such as the Internet is bringing about a fundamental shift in the financial services industry. The providers of Internet banking services must be more responsive towards security requirements. Security threats can affect a financial institution through numerous vulnerabilities. No single control or security device can adequately protect a system connected to a public network. Many problems concerning the security of transactions are the result of unprotected data being sent between clients and servers.

This article discusses the use and safety of electronic banking within defined social groups.

## 1. ELECTRONIC BANKING, ADVANTAGES AND DISADVANTAGES, USE AND SAFETY

According to Polouček et al. (2013), electronic banking can be defined as the provision of banking products and services to clients by means of electronic ways.

Advantages and disadvantages accruing for interested parties in case of the use of electronic banking can be defined as follows.

*The Advantages* of electronic means of communication for the *client*: increased competition is usually transformed into improved quality of services and lower fees for traditional banking services, the client does not need to physically visit the bank, which means, increase of comfort, significantly better availability of banking products and services, saving time and costs compared to physical presence in the bank, fast and unlimited access 24 hours a day.

*The Advantages* of electronic means of communication for the *bank*: lower costs for the Bank (saving capital and operating costs), and by transferring simple banking transactions to a client has opened a room devoted to consultancy for more demanding banking products.

*Disadvantages* of electronic means of communication for the *bank*: high costs of acquisition and operation of the electronic banking system, possible problems of unambiguous identification of a client without personal contact, the potential loss of sales opportunities compared with personal contacts, high demands for safety of communication at all levels.

*Disadvantages* of electronic means of communication for the *client*: the need for appropriate technical equipment and minimal knowledge of the control of technical equipment. (more details: Belás et al., 2010)

According to Koskosas (2011) electronic banking provides tremendous benefits for bank customers in terms of simplicity and transaction costs, but it also presents new challenges for banks in the field

of financial systems, where the design and implementation are necessary to consider safety measures and controls.

Currently banks are intensively using internet technologies and offer customers their banking services through the Internet. Internet banking can be defined as the provision of banking services through a computer network (the internet). It is the most important form of electronic banking at present.

Clients who use internet banking have continuous access to their accounts, at any time and space they may carry out money transfers between accounts, view their bank statements for transactions or to pay their bills and perform other banking transactions electronically through the website of the bank (Yoon and Steege, 2013; Yoon and Occeña, 2014).

Internet banking has created an alternative to visits of the banking branches and from the establishment of a global computer network its use just continues to grow. While in 1993 the Internet was used only by less than 15 million users (0.3% of the world population), in 2014 their number was already around three billion users (40.4% of the world population) (Internet live stats, 2014).

In Slovakia, the Internet users increase was slower than the worldwide trend, but Slovakia now belongs among the countries with the highest penetration of the Internet in the world. In 2014 the internet banking was used by 83% of the population (Internet live stats, 2014).

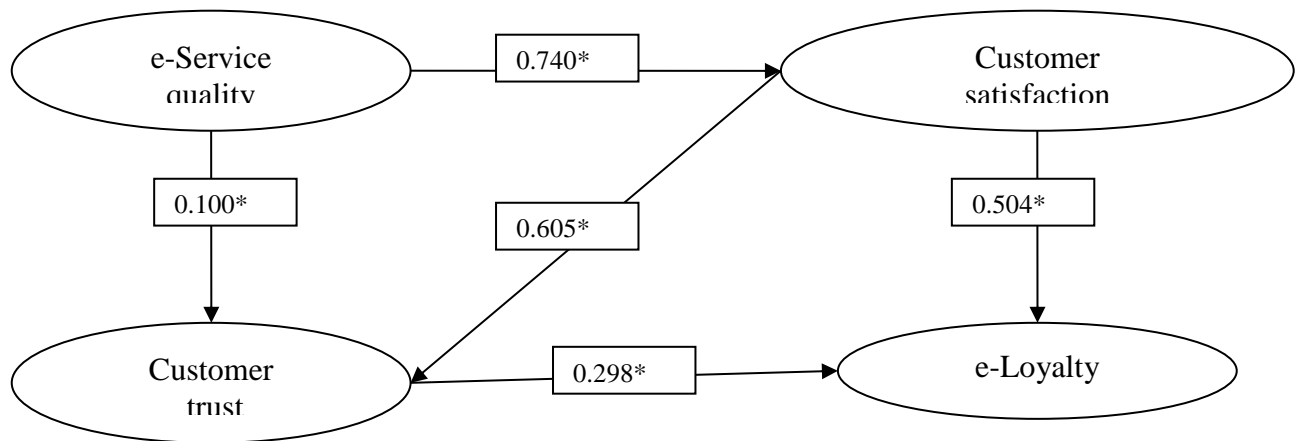
The concept of customer-perceived security is closely linked to the use of electronic banking and it has been shown that it influences the behavior and attitudes of bank customers (Grabner-Krauter and Faullant, 2008). According to Lee (2009), Featherman and Pavlou (2003), the perceived lack of security, defined as the potential loss due to fraud or threat to security through Internet banking. Therefore, Kruck, Gotts, Moghadami, Broom, and Forcht (2002), Flavián and Guinalíu (2006) consider security and privacy as two main prerequisites for trust and confidence in electronic banking (e-banking).

According to Nochai and Nochai (2013) the quality of online banking can significantly enhance customer satisfaction by offering access to a range of financial transactions.

Chu, Lee, Chao (2012) have tested the relationships between service quality, customer satisfaction, customer trust and loyalty in electronic banking. The authors state that if e-banks want to develop strong relationships with their customers, generally this will happen automatically through the provision of excellent e-service quality; e-service quality may even have a direct role in maintaining the customer trust, satisfaction, and loyalty. E-service quality was found to have a strong positive impact on e-loyalty, along with customer satisfaction and customer trust. Quantification of individual bonds is presented in Pic.1.



Figure 1 Links between different variables

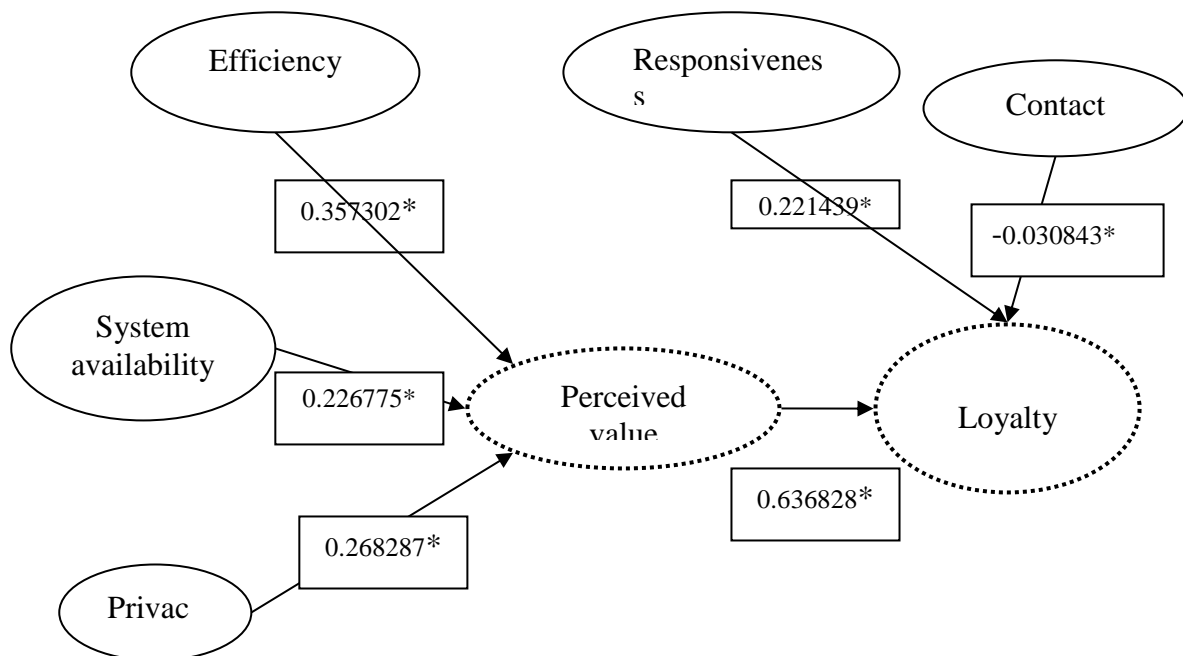


(Source: Chu, Lee, and Chao, 2012)  
Note: \* Correlation coefficient

Marimon, Yaya, Fa (2012) reported that in electronic business there exists a direct relationship between the quality of services (perceived value) and customer loyalty. Efficiency is the most important factor, which generates customer loyalty in the user, the other two factors (system availability and ensuring of privacy) are less important. According to the authors, the effectiveness means that the bank's customer can easily find what it needs, operations are performed quickly, information is well-organized, access to the web is fast, and it is easy to be used as well.

Figure 2 shows the important links between different variables and their quantification.

Figure 2 Significant links between different variables and their quantification



(Source: Marimon, Yaya, and Fa, 2012)  
Note: \* Path coefficient

Chen, Hsiao, and Hwang (2012) reported that IBCS (Internet banking customer satisfaction) model is a model that consists of six major components: content, accuracy, format, ease of use, timeliness

and safety. According to the results of this study IBCS model was significantly emphasizing that consumers are sensitive to Internet safety (safety technology, consumer confidence in internet services).

There are a continuously growing number of customers who use Internet banking because of its convenience. But the security and privacy of Information may be one of the biggest concerns to the Online Banking users. The problem with Online banking applications is that they send data directly to customer in plain text form compromising with security. The solutions to the security issues require the use of software-based solutions that involve the use of encryption algorithms. For this we propose a challenge-based/response-based short-time password authentication methods using Symmetric cryptography in combination with Software Security model (Shazmeen and Prasad, 2012).

Hoffmann and Birnbrich (2012) examined the security attributes of electronic banking. According to the authors, security is a fundamental and increasingly important issue in today's banking industry. Fraud prevention has become a central concern to banks, customers, and public policy makers. Banking fraud hurts both banks and their customers.

Older customers indicate to be more familiar with and have a better knowledge about their banks' fraud prevention measures than younger ones, while the positive effects of knowledge ability on customer relationship quality are significantly lower for the older age group. These findings suggest that perceptions of being well informed and knowledgeable may make older customers more skeptical about the anti-fraud measures employed by their bank than younger customers. Fraud prevention is a crucial aspect in bank relationship for customers across all education and income levels (Hoffmann and Birnbrich, 2012).

## **2. RESEARCH OBJECTIVE, METHODOLOGY AND DATA**

The aim of this article was to examine the selected attributes of security and the use of electronic banking and quantify differences in the approach of clients by gender, education and age.

Within the research we have conducted a questionnaire survey in the Slovak Republic in 2015 on a sample of 321 respondents, of which 61.37% were male and 38.63% were women. The education level of respondents was as follows: most respondents (67.60%) had university education, 27.41% of respondents had secondary education and 4.98% reported that they have a basic education only.

The research was conducted by a random selection. The questionnaire was freely accessible at <http://www.iankety.sk/dotaznik/327968727/>.

In our research 51.71% of respondents were aged 18-35 years and 48.29% of the respondents were aged over 35 years. In our research, we set two fundamental scientific hypotheses. In determining the assumptions we have used findings of cited authors and proceeded with estimation techniques based on their own research:

H1: The use of electronic banking by defined social groups of banking clients is not the same.

H1a: Men, university educated clients and younger customers using electronic banking more in general.

H1b: Men, university educated clients and younger customers using electronic banking more often.

H2: There are differences in opinions within the bank customers in terms of identified social groups to the security attributes of electronic banking.

H2a: Women customers with lower education (not universities), and older clients have a lower level of trust in the security of electronic banking.

H2b: Women, customers with lower education (not universities), and older clients are less likely to connect to the electronic banking services through public networks.

H2c: Women, customers with lower education (not universities), and older clients are less likely to follow current trends in electronic banking.

The validity of each hypothesis was verified by us through the Pearson statistics. This method allows us to quantify statistically significant differences within the defined sets of respondents. Description of Chi - square test of a good correlation is according to Řezánková (2007) approximates as follows. We test the hypothesis  $H_0: \pi_i = \pi_{i,0}$ , where  $i = 1, 2, \dots, K$  ( $K$  the number of categories) a  $\sum \pi_{i,0} = 1$ , against the alternative hypothesis  $H_1: H_0$  does not apply. Unless the constants  $\pi_{i,0}$  are equal, then the null hypothesis could be expressed as  $H_0: \pi_1 = \pi_2 = \dots = \pi_k$ . For  $n\pi_{i,0} \geq 5$  the Chi-square statistics given by the relation is being used:

$$\chi^2 = \sum_{i=1}^K \frac{(n_i - n\pi_{i,0})^2}{n\pi_{i,0}} \quad (1)$$

where:  $n\pi_{i,0}$  is the theoretical (expected) occupancy of the  $i$ -th category in the selection of the range of  $n$ . This random variable has provided the true hypothesis  $H_0$ , chi - square separation with  $(K - 1)$  degree of freedom, i.e.  $\chi^2 \sim \chi^2 [k - 1]$ . Calculated value of the test criterion  $\chi^2$  is therefore could be compared with quintile  $\chi^2_{1-\alpha} [K - 1]$

The validity of each hypothesis, was verified by us through the p-value on a significance level of  $\alpha = 0,5$ . Also the calculated value is greater than 0.05, and  $H_0$  is true. If the calculated p-value is less than 0,05, we did not confirm the validity of  $H_0$  and thus the validity of the hypothesis  $H_1$  can be confirmed.

When calculating the p-values in the chi-square method we have used freely accessible calculator available at: <http://www.socscistatistics.com/tests/chisquare2/Default2.aspx> For the detection of statistically significant differences in the individual answers to the questions we have used freely accessible calculator for calculating the Z-Test available on: <http://www.socscistatistics.com/tests/ztest/Default2.aspx>).

### 3. RESULTS AND DISCUSSION

In Table 1 there are shown the results of research on the use of electronic banking.

**Table 1 Quantitative evaluation of individual social groups in the use of electronic means of payment**

<i>Do you use electronic forms of payment in banking?</i>	Men Count: 197	Women Count: 124	Higher Educated Count: 217	Others Count : 104	Under 35 years Count: 166	Over 35 years Count: 155	p-value Z-test Men/Women HE/Others 35-/35+
1. Yes	180	115	206	89	157	138	0.6599
<i>share in %</i>	91.37	92.74	<b>94.93</b>	85.58	94.58	<b>89.03</b>	<b>0.0041</b>
<i>share in % total=91.90</i>							0.0688
2. No	17	9	11	15	9	17	
<i>Chi square</i>	0.1923		<b>8.2641</b>		3.3122		
<i>p-value</i>	0.6610		<b>0.0040</b>		0.0688		

(Source: own research)

The research results have shown that electronic forms of banking in Slovakia are used by more than 90% of respondents. Within the defined social groups, it was found that the largest share of users of electronic banking in the group of respondents with higher education and the smallest share of users in the group of respondents over 35 years.

The values of test criteria (chi-square and p-value) listed in Table 1 confirmed partial validity of hypothesis H1a. It was found out that there are statistically significant differences in the intensity of use of electronic banking between bank clients with a university degree and customers with other types of education (chi-square = 8.2641 / p-value = 0.0040). P-value of the Z-test (0.0041) showed that higher education clients significantly more use electronic forms of payment than other customers.

The results of our study are compatible with the findings by Internet Live Stats (2014). For example, Ernst & Young (2012) stated that 78 % of customers in the Czech Republic control their bank accounts via Internet. It can be assumed that at present the use of internet banking in the Czech Republic is about the same as in Slovakia. These data confirm the enormous growth of internet banking by users around the world.

The quality of electronic banking considerably determines customer satisfaction with the bank. This fact is confirmed by the results of our previous researches. Survey results for reasons of satisfaction in the Czech Republic present the fact that most clients are satisfied with the possibilities of electronic banking (e-banking). The possibility of using of electronic banking (e-banking) as the most important factor in satisfaction was mostly preferred by women than men, the young people up to 30 years and clients with higher education. In the banking sector of Slovakia the most important factor in satisfaction was the possibility of using of e-banking service, the second most important reason for satisfaction was the availability of the bank's branch and the third most important reason for satisfaction was well developed network of ATMs. This research has shown statistically significant differences in individual social groups. The possibility of using of e-banking service is more significant in Slovakia for younger clients and customers with higher education (Belás, Cipovová, and Demjan, 2014). These findings are similar to findings of Nochai and Nochai (2013), Chu, Lee, and Chao (2012), and Marimon, Yaya, and Fa (2012).

In Table 2 there are presented the results of research on the intensity of the use of electronic banking.

Table 2 The intensity of the use of electronic banking

How often do you use electronic banking (EB)?	Men	Women	Higher Education	Others	35-	35+	p-value M/W /Others 35-/35+
1. Daily share in % share in % totally=61.37	118 59.90	79 63.71	143 <b>65.90</b>	54 51.92	109 65.66	88 56.77	0.4965 <b>0.0160</b> 0.1031
2. Once a week	67	38	69	36	50	55	
3. Once a month	7	4	5	6	4	7	
4. Never	5	3	0	8	3	5	
Chi square/ p-value	0.4715 0.9251		<b>21.5639</b> <b>8E-05</b>		3.4219 0.3310		

(Source: own research)

In our research, it was found out that up to 65.90% of Slovakian university graduates banking customers are using electronic banking daily. The average intensity of daily use of electronic banking is relatively high, and this is confirmed by the number of 61.37%.

H1b was partially confirmed, because we found that university education clients significantly more use electronic banking on a daily basis. When compared by gender and age, we did not find any significant differences in daily use of electronic banking.

Within the H1, we assumed that the use of electronic banking by the social groups defined by bank customers is not the same. Our research confirmed partially the validity of hypothesis H1 (clients with higher education to a greater extent and more intensively use electronic banking).

In Table 3 we present the results of research in which the clients evaluated the safety of electronic payments.

Table 3 Security of payments through electronic banking

Do you believe that the payments through EB are safe?	Men	Women	Higher Education	Others	Under 35 years	Over 35 years	p-value M/W /Others 35-/35+
1. Yes share in % share in % totally=78.19	159 80.71	92 <b>74.19</b>	174 80.18	77 74.04	135 <b>81.33</b>	116 74.84	0.1676 0.2113 0.1585
2. No	38	32	43	27	31	39	
Chi square p-value	0.4689 0.4935		1.6507 0.1989		2.0129 0.1560		

(Source: own research)



Confidence in the security of payments via electronic banking varies within the groups surveyed from 74.19% (women) to the value of 81.33% (young customers). The overall proportion of clients who believe in the security of electronic payments was at the level of 78.19%.

H2a has not been confirmed, because we did not find any statistically significant differences between social groups of bank customers.

In Table 4 there are presented the results of research on how defined social groups accessing the security attributes, and its whether they connect to the electronic banking in public networks.

**Table 4 The use of electronic banking through public networks**

<i>Do you connect to the EB through the public networks?</i>	Men	Women	Higher Education	Others	35-	35+	p-value M/W HE/Others 35-/35+
1. Yes	52	29	57	24	52	29	0.5485
<i>share in %</i>	26.40	23.39	26.27	23.08	<b>31.33</b>	<b>18.71</b>	0.5353
<i>share in % totally=25.23</i>							<b>0.0093</b>
2. No	145	95	160	80	114	126	0.5485
							0.5353
							<b>0.0093</b>
<i>Chi square</i>	0.3652		0.3793		<b>6.7619</b>		
<i>p-value</i>	0.5456		0.5380		<b>0.0093</b>		

(Source: own research)

In our research, we found out that the proportion of clients who use public networks to connect to the Internet was 25.23%, which can be seen as prudential behavior of banking customers in Slovakia.

H2b hypothesis was partially confirmed. In our research, we found out that the clients up to 35 years more frequently were using the connection to electronic banking through public networks when compared to older customers (p-value=0.0093).

In Table 5 there are presented the results of research on how defined social groups follow current trends in the field of security of electronic banking.

Table 5 Trends in area of security of cashless payment transactions

<i>Do you follow current trends in security of EB?</i>	Men	Women	Higher Education	Others	35-	35+	p-value M/W HE/Others 35-/35+
1. Yes <i>share in %</i> <i>share in %</i> <i>totally=46.73</i>	97 49.24	53 42.74	108 <b>49.77</b>	42 <b>40.38</b>	75 45.18	75 48.39	0.2543 0.1141 0.5619
2. No	100	71	109	62	91	80	0.2543 0.1141 0.5619
<i>Chi square</i> <i>p-value</i>	1.2903 0.2560		2.4876 0.1147		0.3310 0.5650		

(Source: own research)

According to our research the current trends in the area of electronic banking are monitored by 47% of bank customers. The largest share of bank clients we have discovered in the segment of university educated respondents (49.77%) and the smallest in the group of clients with lower education (40.38%).

H2c has not been confirmed, because we did not find any statistically significant differences between individual social groups.

Within H2 we assumed that there are differences in the views of the bank customers on security attributes of electronic banking by gender, education and age of the respondents. Our research confirmed the validity of H2. It was found out that the selected attributes of electronic banking are perceived almost equally by the defined social groups of banking customers.

In our research we have also found out that up to 83.18% of customers rely on security measures of the bank's online banking and 87.23% of respondents have a negative experience in hacking attacks or of fraud while utilizing banking services.

According to Furnell, Bryant, and Phippen (2007) the internet represents now the greatest potential threat of attacks on clients of commercial banks. Customers are very well familiar with the internet threats, and they also realize that it is their own obligation to protect against these menaces, even though they have no confidence and knowledge to do so. Via various techniques hackers are trying to get sensitive information from customers of banks with the purpose of abusing them. In recent years, the attacks on electronic banking have increased significantly, while threatening especially bank customers, their personal details and financial resources.

According to Kaspersky Lab company (2014), an organized gang of computer hackers who from the end of 2013 attacked a hundred of banks in 30 countries (Russia, USA, Germany, China, Ukraine, Canada, Hong Kong, Taiwan, Romania, France, Spain, Norway, India, Great Britain, Poland, Pakistan, Nepal, Morocco, Iceland, Ireland, Czech Republic, Switzerland, Brazil, Bulgaria and Australia), has stolen in illegal operations for over a billion US dollars.

These findings are compatible with the conclusions of Chen, Hsiao, and Hwang (2012) and Hoffmann and Birnbrich (2012).

In this context Fatima (2011) states that financial institutions that offer Internet-based products and services should have reliable and secure methods to authenticate their customers. The level of authentication used by the financial institution should be appropriate to the risks associated with those products and services. Biometric based authentication and identification systems are the new solutions to address the issues of security and privacy. Biometrics is finding its way into all kinds of applications beyond access control. It is expected that more and more information systems/computer networks will be secured with biometrics with the rapid expansion of Internet and Intranet.

The future of electronic banking will be a system where users are able to interact with their banks “worry-free” and banks are operating under one common standard. Most research studies have indicated that the common problem affecting information security and privacy of customers is e-services provider’s lack of security control which allows damaging privacy losses. Apart from that, another problem is the subsequent misuse of consumers’ confidential information, as in identity theft. These may affect customer’s confidence toward online business transaction in a variety of privacy risk assessments by consumers. Current technology allows for secure site design. It is up to the development team to be both proactive and reactive in handling security threats, and it’s up to the consumer to be vigilant when doing business online (Omariba, Masese, and Wanyembi, 2012).

## CONCLUSION

Electronic banking represents an important area of business activities of commercial banks. Client access to banking services through electronic distribution channels represents a significant current trend, which determines the satisfaction of bank customers. An important attribute of electronic banking is its safety.

The results of our research have confirmed that the dominant part of bank customers uses electronic access when managing their personal finances. We found out that there are some differences in the approach of bank customers as per their education level. Clients with higher education to a greater extent and more intensively use electronic banking.

In the safety area, we did not find any significant differences between banking clients by gender, education and age. The only exception is the finding that clients up to 35 years are significantly more confident while using electronic banking through public networks.

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<http://www.socscistatistics.com/tests/chisquare2/Default2.aspx>

<http://www.socscistatistics.com/tests/ztest/Default2.aspx>



## ARE MEN MORE INNOVATIVE AND AGGRESSIVE IN BUSINESS? CASE STUDY FROM THE CZECH REPUBLIC

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### ABSTRACT

*SMEs make a major contribution to the growth and employment in the EU. In today's fierce competition in the market economic activities the SMEs had gradually developed into a major force for national economic and social development in every country of world. The aim of this article is to examine the approach to innovativeness and competitive aggressiveness between males and females in the segment of small and medium-sized enterprises. Based on the results of the questionnaire which was conducted in May 2015 in the Czech Republic we tried to test four hypotheses on the relationship between the gender of entrepreneurs of SMEs and their attitude to innovativeness and competitive aggressiveness. The results of our research have pointed out some differences between genders. Men-entrepreneurs who do business in the segment of SMEs in the Czech Republic are slightly more innovative and are significantly more aggressive in regard to competitors than women, as they apply aggressive approach and their companies are perceived as aggressive.*

### KEY WORDS

*Small and medium-sized enterprises, gender, innovativeness, competitive aggressiveness*

### JEL CLASSIFICATION

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### INTRODUCTION

The issue of business risks of the small and medium enterprises (SME) currently represents contemporary area of theoretical research and practical applications.

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Small and medium-sized enterprises (SMEs) in general and the establishment of new enterprises in particular play an important role in creation and keeping of a functioning market economy, especially as a means of stimulating competition, creating jobs and promotion of the economic recovery (Kessler, 2007). SMEs are considered to be important generators of economic development, which contribute to addressing the economic, political and social problems of the state. They include the vast majority of private sector enterprises and ensure more than 50% of employment and manage economic growth. On the other hand, due to their size, they often face both internal (lack of management skills) and external (unfavorable market conditions and institutional settings) obstacles that may hinder their further growth. (Hessels, Parker, 2013)

Our article is devoted to the differences in approaches of men and women in the field of innovation activities and aggressiveness to competitors.

## 1. THEORETICAL BACKGROUND

*Entrepreneurial orientation* is a key element for the success of SMEs (Brockman, Jones, and Becherer, 2012; Boso, Story, and Cadogan, 2013). To behave entrepreneurially means the company should engage in these strategic activities— innovativeness, competitive aggressiveness, proactiveness, risk taking, autonomy. (Anderson and Eshima, 2013; Sidik, 2012)

According to Gudmundson and Lechner (2014) entrepreneurial orientation has a positive effect on the firm performance with both cost leadership and differentiation strategies. Their result shows that innovativeness and autonomy has a positive relationship with product differentiation strategy whereas risk taking and competitive aggressiveness has a negative relationship with innovativeness, but no significant relationship was found with proactiveness. The findings of Moreno and Casillas (2008) showed that higher entrepreneurial orientation favors the strategies through product and process innovation, thus entrepreneurial orientation will have impact on the firm innovations strategies that can support launching new products rather than entering to new market segments.

Kraus (2013) states that there is a significant relationship between firm performance and entrepreneurial orientation of the entrepreneur. More experienced entrepreneurs are more inclining to risks, more innovative and proactive within their organization. Similarly Blackburn, Hart, and Wainwright (2013) found out that small business performance is largely depended on the business strategies, age of the business, size of the business and entrepreneurial characteristics and entrepreneurs with high risk tolerance, innovativeness and willingness to use new technologies are more successful in generating profits for the firm.

*Innovativeness* reflects the tendency of companies to promote new ideas, innovations, experiments and creative processes that can result in new products, services or technological processes. According to Lasagni (2012) the innovation performance is higher in SMEs that are proactive in strengthening their relationships with innovative suppliers, users, and customers. Martínez-Roman and Romero (2013) have found out that SMEs that have introduced their substantial product innovations are led by the businessmen with a large internal motivation. Boyer and Blazy (2014) examined the determinants of survival of non-innovative and innovative enterprises; the survival of these companies is associated with personality characteristics, such as gender, age, association with a national minority, professional experience and financial resources.

*Competitive aggressiveness* perceived as a further element of business orientation is according to Lumpkin and Dess (1996) related to the companies' qualities and direct and intensive challenge of the competitors in order to enter the market or to improve the markets' position, i.e. to fulfill the role

of rivals in the market. It is typical, for the company to react in a way which may be considered as a direct confrontation, for example when the company enters the market dominated by another competitor or it behaves reactively for example when the company reduces the price in response to the competitor appeal.

Soininen, Puumalaiene, Sjogren, and Syrja (2012) analysed the role of entrepreneurial orientation in global economic crisis. By using a sample of 194 SMEs in the Finnish market they have found that entrepreneurial orientation namely innovativeness and pro-activeness indeed played a crisis mitigating role in the crisis period. They found a negative effect of risk taking and financial as well as operational performance. It means that those firms that are more risky have suffered more in the financial crisis period than the firms those are risk averse. The profitability and liquidity measures of risk taking also show that during the financial crisis their profitability and liquidity reduced a lot for the high risk taking firms. Nevertheless, innovativeness and pro-activeness positively affected the firm's assets and revenues, but they did not find any evidence for the liquidity and profitability. The results provide support for firms with entrepreneurial orientation, because innovative and pro-active firms can launch new product and services for their customer to maintain the operational balance and the financial stability. More risk taking firms are uncertain and they are financing to utilize the leverage. On the other hand, innovative and pro-active firms are taking initiatives to utilize their own resources that can create a complete edge over their rivals in terms of resource utilization. Thus, firms with more EO can have more smoothed growth than firms with lower EO, due to balancing nature of risk taking and more innovativeness and pro-activeness.

Examining of identical and different features between the two genders belongs to the important areas addressed by several authors. According to Mueller and Dato-on (2010) women play an important role in the growth of businesses worldwide, but there is still a considerable difference in participation rates. Similarly International Finance Corporation (2013) states that female entrepreneurs greatly contribute to the formal economy. An estimated 31 to 38 percent of formal SMEs in developing economies are fully or partially owned by women.

Gender influences the extent of participation in business and an approach to risk assessment. Studies show that there are a lot of differences between male and female entrepreneurs. Understanding of success is one of the examples. Women understand success as the ability to take control of their destiny, build relationships with prospective clients and do things that fulfil them, while men define success as achieving the objectives. In this context Millian, Congregado, Roman, Van Praag, and Van Stel (2014) state that men entrepreneurs can have higher incomes than women entrepreneurs. Moreover, there is a chance that women can leave the venture due to family issues and or age.

According to Goktan and Gupta (2015) individual entrepreneurial orientation is higher among men rather than women. They find that men are much more innovative, risk taking incentives and proactive in entrepreneurship development. At the same time they enhance that people having masculine values are competitive, aggressive and they are motivated to gain wealth, through business development.

Langowitz and Minniti (2007) found out that women are more risk averse than men, and that higher riskiness does not prevent men from starting the business. This finding confirm Diaz-Garcia and Jimenez-Moreno (2010) and at the same time they state that females are more innovative and objective in achieving task and men are likely have a thought about the intention to create a firm rather than doing it in practically. Also Runyan, Huddleston, and Swinney (2006) found out that females are more innovative than their males counterpart, but on the other hand in risk taking females scored more than the males and there were no significant differences found in proactiveness. Compared to Ayub, Razzaq, Aslam, and Iftekhar (2013) their results show that

women have lower innovativeness and autonomy, but are more proactive and risk averse and less aggressive than men. The research by Kozubíková and Bartos (2015) and Kozubíková, Belas, Bilan, and Bartos (2015) provides interesting results in this context.

Women-owned SMEs face the same challenges as every other SME. However, these challenges are usually amplified, and/or harder to overcome. And these seem to reflect the size of women-owned enterprises: they are mostly very small and small firms. Is this by their choice, or are women entrepreneurs specifically constrained? In terms of access to finance there is evidence that women entrepreneurs have a disadvantage compared to their male counterparts. Access to finance by women-owned enterprises is constrained by legal and regulatory environment, firm specific/owner-specific characteristics (e.g. education, training, size of firm, etc.), and cultural barriers, which may impact women entrepreneurs disproportionately, in addition to other barriers to access faced by SMEs in general. (International Finance Corporation, 2013)

Global Markets Institute (2014) submits similar conclusions. Women-owned SMEs face barriers to entry and the growth of business that include access to education and training, legal and cultural barriers and infrastructure-related challenges. Access to finance is typically identified as a critical constraint. While financing is almost always a challenge for SMEs, the difficulties are often intensified by gender-related factors, including women's lack of collateral, weak property rights and discriminatory regulations, laws and customs.

In this context we emphasize that access to external financing significantly determines the success of innovation policy of the company.

Inspirational conclusions can be found in the studies by Envick and Lim (2011). Authors state that there is a significant difference in risk taking among the male and female respondents. The potential male entrepreneurs are ready to accept more risk than the female entrepreneurs, it is suggested that females are more risk adverse than their male counterparts. It is also found that, in the USA and Korea males are more independent decision makers than females, however, the result is less significant for Malaysia and Fiji. Males are more confident in their decision making than females in all the four countries surveyed. It is also noticeable that females are less aggressive in the competitiveness rather than males. Whereas males prefer to be more aggressive when they find any competitive opportunity to enter the market. Females are not interested in the growth of their firms, they are happy with their stable condition. However, females are found to be more innovative than males, which is one of their advantages in the formation of new enterprise in comparison to males.

## **2. OBJECTIVES, METHODOLOGY AND DATA**

The aim of this article is to examine the approach to innovativeness and competitive aggressiveness between males and females in the segment of small and medium-sized enterprises (SMEs).

The research of the business environment was prepared in 2014 and was conducted in the Czech Republic in 2015. The companies were chosen from Albertina database. The total number of 1,650 randomly selected firms was addressed by e-mail or telephone to fill in the questionnaire placed at website

[https://docs.google.com/forms/d/1U9coaC5JRL0N2QOOO6Xb8j3mnaZXdSM47Kugt4EDGFo/vie/wform?usp=send\\_form](https://docs.google.com/forms/d/1U9coaC5JRL0N2QOOO6Xb8j3mnaZXdSM47Kugt4EDGFo/vie/wform?usp=send_form). The data was provided by 1,141 owners of SMEs in 14 regions of the Czech Republic. The questionnaire consisted of 52 questions. In this context, in the first nine questions we devoted to the analysis of the structure of the respondents in relation to their education, gender, age, the residency and size of a firm, the length and area of conducting business, motives for starting a business and the most important characteristics of entrepreneur. The rest of

questions were scale questions of the scale of 1 to 5 (1 - fully agree, 2 – agree, 3 - no position, 4 - disagree, 5 - completely disagree) focused on the five elements of entrepreneurial orientation.

The structure of the sample according to the business area was as follows: trade companies (33%), manufacturing companies (23%), construction companies (14%), transport companies (6%) and agricultural firms (3%). The largest portion of companies operated in other sectors (39%). In accordance to the length of doing business from the total number of 1,141 companies 62% of them were doing business for more than 10 years, 21% of them between 1 and 5 years, and 17% of them between 5 and 10 years. It can be said that the owners of the companies were quite experienced entrepreneurs. 65% of firms were micro-enterprises, 27% were small enterprises and 8% were medium-sized enterprises. Most of the entrepreneurs in the sample, concretely 48% had secondary education with graduation, 34% of them had a college education and 18% had secondary education without graduation. In relation to the gender of the entrepreneur from total number of firms 75% of them were men and 25% of them were women.

In line with previous findings and taking in account the gender we have stated the following hypotheses:

H1: More than 60% of entrepreneurs said they regularly develop new products. There are statistically significant differences between men and women.

H2: The innovative activities of the companies are severely limited due to the influence of the crisis. A maximum of 40% of entrepreneurs they have invested a lot of money into the development of new methods and technologies. There are statistically significant differences between men and women.

H3: A maximum of 20% of entrepreneurs agree with the statement that their firm has a reputation of aggressive company. There are statistically significant differences between men and women.

H4: A maximum of 20% of entrepreneurs agreed with the statement that often apply aggressive practices to the competition. There are statistically significant differences between men and women.

The associations in contingency tables were analyzed by Pearson statistics for data counting. P-value has been compared to standard 5% confidence level. P-value that is lower than the confidence level leads to the adoption of our hypothesis. The calculations have been performed using software available at <http://www.socscistatistics.com/tests>. Statistically significant differences in the affirmative replies were analyzed through Z-score. Calculations were made by the free software available at <http://www.socscistatistics.com/tests/ztest/Default2.aspx>. Part of the quantitative analysis is the use of indicators and descriptive statistics such as the percentage figures.

### **3. RESULTS AND SHORT DISCUSSION**

Table 1 presents the results of our research among entrepreneurs in the segment of SMEs. The following table sets out the views of male and female entrepreneurs.



**Table 1. The opinion of SMEs entrepreneurs in relation to regular development of new products and services in their firms**

<i>We regularly develop new products and services in my company.</i>	men in %	women in %	p-value Z-score
1. Fully agree	9.99	13.57	0.0949
2. Agree	50.75	51.07	0.9283
Share in % (1+2)	60.74	64.64	0.2420*
Total share in % (1+2) = 61.70			
3. No position	20.09	17.50	0.3421
4. Disagree	15.56	15.71	0.9522
5. Completely disagree	3.61	2.14	0.2301
$\chi^2 = 4.6177 / p\text{-value} = 0.3288$			

(Source: own calculation).

Note: \* means p-value of the Z-score calculated from the positive answers (1 + 2)

In our research we found that 61.70% of entrepreneurs regularly develop new products, which means that the first part of H1 was confirmed. The second part H1 was not confirmed. We found that there weren't statistically significant differences between men and women in the development of new products. *So H1 was partially confirmed.*

Table 2 presents the results of the research in the field of investing money into new methods and technologies, and comparison between men and women.

**Table 2. The opinion of SMEs entrepreneurs in relation to the investment into new methods and technologies**

<i>We invest a lot of money into the development of new methods and technologies</i>	men in %	women in %	p-value
1. Fully agree	4.76	6.43	0.2757
2. Agree	33.22	31.43	0.5823
Share in % (1+2)	37.96	37.86	0.9203
Total share in % (1+2) = 37.60			
3. No position	25.55	27.86	0.4473
4. Disagree	30.89	29.64	0.6965
5. Completely disagree	5.58	4.64	0.5485
$\chi^2 = 2.2228 / p\text{-value} = 0.6949$			

(Source: own calculation).

Our assumption that the innovative activities of the companies are severely limited due to the influence of the crisis was confirmed, because only 37.60% of entrepreneurs reported that they have invested a lot of money into the development of new methods and technologies. We found that there weren't statistically significant differences between men and women in this area. *H2 was partially confirmed.*

The most important business risks which were perceived by entrepreneurs in the Czech Republic in our previous research were as follows: market, financial and personnel risks. Market risk was

identified as a key risk by the largest number of entrepreneurs - 79.44% of them in the Czech Republic (Belás et al., 2014 ). The situation is similar in Slovakia, where it was found out that the most important business risk was market risk (average value of perceived market risk was higher than 50%). (Belás, Bilan, Ključnikov, Vincúrová, and Macháček, 2015)

The research results showed that men are slightly more innovative in developing new products and that both genders have the reserved attitude to the financial investment in the development of new methods and technologies.

Our results in terms of innovativeness of men and women did not confirm the conclusions of Diaz-Garcia and Jimenez-Moreno (2010), Runyan et al. (2006), Ayub et al. (2013). Our research confirmed the findings by Lim and Envick (2011).

In Table 3 sets out the views of entrepreneurs on whether their company is perceived as aggressive company.

**Table 3. The opinion of SMEs entrepreneurs in relation to the perception of their firms as an aggressive firm**

<i>Our company has a reputation as an aggressive company.</i>	men in %	women in %	p-value
1. Fully agree	1.86	0.71	0.1835
2. Agree	9.87	6.43	0.0801
Share in % (1+2)	11.73	7.14	0.0300
Total share in % (1+2) = 10.60			
3.No position	25.44	19.29	0.0357
4.Disagree	49.59	56.43	0.0466
5.Completely disagree	13.24	17.14	0.1031
Share in % (4+5)	62.83	73.57	0.0010**
$\chi^2 = 12.0600 / p\text{-value} = 0.0169$			

(Source: own calculation).

Note: \*\* means p-value for the answers 4+5.

H3 was confirmed. We found that only 10.60% of all entrepreneurs agreed with the statement that their company has a reputation for aggressive company.

Values of the test criteria (chi square = 12.0600 / p-value = 0.0169) confirmed that there are statistically significant differences in the overall responses of men compared to women. At the same time we found that there were statistically significant differences between men and women in the affirmative replies (p-value (1 + 2) = 0.0300). Significantly more men-businessmen presented the view that the company has a reputation as an aggressive company. Women compared with men reported significantly more that their company does not have a reputation for aggressive firms (p-value = 0.0010)

In Table 4 presents the results of the research on aggressive activities that are directed against competitors.

**Table 4. The opinion of SMEs entrepreneurs in relation to realizing aggressive activities against the competition**

<i>Our activities in relation to competition are often aggressive.</i>	men in %	women in %	p-value
1. Fully agree	1.97	0.71	0.1527
2. Agree	11.50	9.64	0.3898
Share in % (1+2)	13.47	10.36	0.1738
Total share in % (1+2) = 12.71			
3. No position	20.67	15.71	0.0688
4. Disagree	55.52	59.29	0.2713
5. Completely disagree	10.34	14.65	0.0489
Share in % (4+5)	65.86	73.94	0.0121**
$\chi^2 = 9.3148 / p\text{-value} = 0.0537$			

(Source: own calculation).

We found in our research that only 12.71% of all entrepreneurs reported that they used some aggressive practices against competition.

The values of the test criteria (chi square = 9.3148 / p-value = 0.0537), which are on the borderline of acceptability confirmed that there are statistically significant differences in the overall responses of men compared to women. At the same time, we found that there were statistically significant differences in negative responses between males and females (p-value = 0.0121). Significantly more female entrepreneurs presented the view that their company does not use aggressive practices against competition. *H4 was confirmed.*

Our results in the aggressiveness of men and women confirmed the findings by Goktan and Gupta (2015), Lim and Envick (2011), and Ayub et al. (2013).

According Blackburn, Hart, and Wainwright (2013) entrepreneurs with high risk tolerance, innovativeness and willingness to use new technologies are more successful in generating profits for the company (Laforet, 2013 presents similar conclusions presented in his study). They have also shown that, larger firms' growth rate is lower than the small firms' in terms of employee turnover and employment growth. The reason is that small firms are more flexible and when they find any new opportunity they hire new employees to penetrate the market. While controlling for sector differences, the results show that manufacturing firm's growth rate is lower than the service firms'. However, they find that when taking into consideration the size of the firm the innovative entrepreneurial firms outperform the other firms. More precisely, innovative entrepreneur perform 1.6 times better than other entrepreneurs. Finally, they find that, older firms, smaller in size, perform better than large firms in terms of profitability. It suggests that small firms are very careful about the growth and expansion of the business. They will expand the business, when they are much more certain that, they will have steady earnings from the expansion.

## CONCLUSION

The results of our research have pointed out some differences between the genders. We could present our conclusions that men entrepreneurs doing business in the segment of SMEs in the Czech Republic are slightly more innovative and are significantly more aggressive in relation to competitors, because they apply more aggressive approach and their companies are perceived as aggressive.

The results confirmed that both male and female entrepreneurs in the Czech Republic are trying to implement innovation policy in their companies. 60.74% of male respondents and 64.64% of women respondents are regularly developing new products and services in their companies, which is an important element of business orientation.

The research results have shown differences between men and women in the field of the aggressive business. Significantly more male entrepreneurs presented the view that their company has a reputation as an aggressive company. Women compared with men reported significantly more that their company does not have a reputation of aggressive company, and reported the opinion that their company did not use aggressive practices against competition more often.

Although it is clear that there are certain limits in our research (e. g. uneven representation of respondents by region and gender), we expect that our article has brought interesting findings and new incentives for further research, not only gender but also other socio-demographic factors influencing individual constructs of the entrepreneurial orientation.

In the future our research will concentrate on examination of other socio-demographic factors influencing the entrepreneurial orientation of SMEs in the Czech Republic.

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## CORPORATE GOVERNANCE QUALITY ON SPECIFIC CASE OF ROMANIAN LISTED COMPANIES

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### ABSTRACT

*The purpose of this paper is to analyse the compliance of Romanian listed companies with corporate governance codes. From 2010, the “Comply or Explain” Statement, which discloses if and how the corporate governance principles are applied, became mandatory for all companies listed on Bucharest Stock Exchange (BSE). The methodology employed is based on the analysis of the above mentioned Statements published for the period 2009-2013. Research aims to present through a longitudinal and qualitative study the evolution of the compliance with the BSE Corporate Governance Codes. Most of the observed companies made a step forward in what concerns corporate governance principles and over the study period they disclosed more information on their statements. On the other hand, we found cases where the statements made over the studied period contained inconsistencies for some principles. The implementation of corporate governance rules ensures transparent decision-making, based on clear rules and objectives, and increases shareholders’ confidence in the company.*

### KEY WORDS

*Corporate governance, comply or explain, listed companies, emerging economies, Romania.*

### JEL CLASSIFICATION

*G39*

### INTRODUCTION

Corporate governance is a highly debated and interesting topic that represents a pylon in companies’ life. We can say that good corporate governance is a bridge between management and

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shareholders/stakeholders that leads to transparency and the improvement of financial reporting process.

An outstanding issue of corporate governance, that needs to be debated, is the “comply or explain” principle. The concept of comply or explain has an important impact in Europe since 2006 when the European Commission (EC) introduced comply or explain for the first time in European law, issuing Directive 2006/46/EC of the European Parliament and of the Council that has been implemented by the vast majority of Member States (Keay, 2014, p. 282).

According to the European Corporate Governance Forum (ECGF) for the “comply or explain” principle to be applied, three elements must be present, namely: a real obligation to comply or explain; a high level of transparency, with coherent and focused disclosures; and a way for shareholders to hold company boards ultimately accountable for their decisions to comply or explain, and the quality of their disclosures (Statement of the European Corporate Governance Forum on the comply-or-explain principle, 2006, p. 1). A basic component of this principle is the public Statement concerning compliance or non-compliance of the companies with corporate governance codes.

The purpose of this paper is to analyze the compliance of Romanian listed companies with corporate governance codes. From 2010, the “Comply or Explain” Statement, which discloses if and how the corporate governance principles are applied, became mandatory for all companies listed on Bucharest Stock Exchange (BSE). Before this mandatory application, we can specify that, from our analysis of official document and websites, only a company from non-financial sector (C.N.T.E.E. Transelectrica) has voluntarily presented this statement.

## **1 LITERATURE REVIEW**

In this segment of corporate governance that we analyze in our study, referring to “Comply or Explain” Statement/principle, we found different studies and opinions about the compliance with code provision. Some papers present the companies compliance with the recommendation of governance codes and, on the other hand, other articles present an analysis of the reasons for non-compliance and deviation from code provision, that in many cases are not sufficiently substantial or accurate. One of these studies is conducted by Campbell et.al. (2009) who analyzed the reasons for non-compliance of Polish listed companies based on 250 publicly available compliance statements filed in 2005 by the companies listed on Warsaw Stock Exchange.

In a more recent study, Keay (2014, p. 288) presented on his paper, at the section “statement associated with comply or explain”, some diversity and significant opinions of others scholars about the percentage of companies’ compliance with code provisions.

Luo and Salterio (2014, p. 460) construct in their paper named “Governance Quality in a “Comply or Explain” Governance Disclosure Regime” a board score measure based on the Canadian code’s 47 “best practices”, using the Canadian “comply or explain” corporate governance disclosure regime. This study represent an empirical analysis based on Tobin’s Q proxy for one-year data from 2006. They found that this measure is strongly and positively associated with higher firm value and weakly and positively associated with better operational performance.

Salterio et. al. (2013) developed an analysis of best practices compliance by 742 Canadian public companies with the recommendations imposed by the Canadian Securities Administrators, that are voluntary adopted or explained. Authors compared this rate of compliance (39% of companies completely compliant) with the one from 1334 Australian companies (74% of companies

completely compliant). They analysed sixteen corporate governance best practices that are common to the Canadian and Australian codes of governance. In conclusion they noticed that compliance by adoption of best practice is more common in Canada, whereas compliance by explanation is more common in Australia.

In their working paper No. 389 that was part of CBR Research Programme on Corporate Governance, Seidl et al. (2009) analyzed the compliance statements and reports of 257 largest listed companies in the UK (London Stock Exchange) and Germany (Frankfurt Stock Exchange). This empirical study is based on a derived taxonomy of forms of “explanation” presented in “Comply or Explain” statements that have been divided in two categories: one for full compliance and one for full non-compliance. The authors found these forms of “explanation” based in part on different logics of argumentation, and shows significant divergence in compliance patterns in the UK and Germany (about 60% had at least one deviation from the code provision) which may be explained by differences in experience, culture and legal system (Seidl et.al., 2009).

Study on the mandatory disclosure of accounting information is extremely popular in theoretical studies (e.g. Lee and Tweedie, 1975; Arnold and Moizer, 1984; Abu-Nassar and Rutherford, 1996). These studies deal with specified regulations providing the format of provided information as well as the variety in data covered by the financial statements. According to Healy and Palepu (2001) these are the major factors affecting the managers’ disclosure decisions: (1) capital market transactions, (2) corporate control contests, (3) stock compensation, (4) litigation, (5) proprietary costs, and (6) management talent signaling.

In December 2014 came in force an update of accounting Directive 2013/34/EU on Disclosure of Non-Financial and Diversity Information by Certain Large Companies. Based on the Brussels view, first company reports including such information shall be published in 2018 covering financial year 2017-2018 (Strouhal et al., 2015). According to this directive management report of large companies shall also cover corporate governance statement providing at least the following information:

- (a) a reference to the following, where applicable:
  - (i) the corporate governance code to which the undertaking is subject,
  - (ii) the corporate governance code which the undertaking may have voluntarily decided to apply,
  - (iii) all relevant information about the corporate governance practices applied over and above the requirements of national law,
- (b) where an undertaking departs from a corporate governance code, an explanation by the undertaking as to which parts of the corporate governance code it departs from and the reasons for doing so; where the undertaking has decided not to refer to any provisions of a corporate governance code, it shall explain its reasons for not doing so;
- (c) a description of the main features of the undertaking's internal control and risk management systems in relation to the financial reporting process;
- (d) the information required by Directive 2004/25/EC on takeover bids;
- (e) unless the information is already fully provided for in national law, a description of the operation of the shareholder meeting and its key powers and a description of shareholders' rights and how they can be exercised;
- (f) the composition and operation of the administrative, management and supervisory bodies and their committees; and
- (g) a description of the diversity policy applied in relation to the undertaking's administrative, management and supervisory bodies with regard to aspects such as, for instance, age, gender, or educational and professional backgrounds, the objectives of that diversity policy, how it has been implemented and the results in the reporting period. If no such policy is applied, the statement shall contain an explanation as to why this is the case.

## 2 RESEARCH DESIGN AND METHODOLOGY

The methodology employed is based on the analysis of the “Explain or Complain” Statements published for the period 2009-2013. This research aims to present through a longitudinal and qualitative study the evolution of the compliance with the Bucharest Stock Exchange (BSE) Corporate Governance Codes.

In order to achieve our goal, we select only the companies listed at premium (first tier) category at Bucharest Stock Exchange (BSE) in order to have a homogeneous sample and because the probability to have the “Explain or Complain” Statements and all the information that we need in this analysis on the companies websites is higher. Also we consider that these companies have been adopted in a voluntary way and complied with the BSE Corporate Governance Code. Therefore, the selected sample is formed from 22 companies (10 belonging to the financial sector and 12 non-financial sector companies). According to the BSE Press Release from December 2014, since 15 January 2015 BSE has a new market segmentation, the first category was replaced with the premium one and the second and third categories were replaced with the standard ones ([www.bvb.ro](http://www.bvb.ro)).

Sources where we found the "Comply or Explain" Statement for the analysis period from 2009 and at the most recent version (2013), are the official data published by listed companies on their websites (see Appendix 2), such as the Annual Report, the Supervisory Board's Report, Corporate Governance Code and Bucharest Stock Exchange (BSE) website.

We further developed a disclosure scoring criteria awarding scores of 1-3 based on a Likert scale for items disclosed and '0' otherwise. Therefore, codifying the responses presented in "Comply or Explain" Statement we have the following possibilities:

0 - full non-compliance or not applicable. Some companies specify that for them some principle/recommendation from Corporate Governance Code is not applicable (N/A) or they responded with “No” or “No, not in scope” without giving an explanation for non-compliance.

1 - non-compliance, but explained. In this category we inserted the negative responses with meaningful and plausible explanation.

2 - partial compliance. We codified with 2 the affirmative but not complete responses, for example “Yes, work in progress” or those cases where only a part of recommendation is applied.

3 - full compliance.

We assume the fact that these statements were made correctly, according to the Corporate Governance Code, Constitutive Act and other important statements of companies.

Then, we calculated the percentage score for each company per years based on the above codification and by using the following formula:

$$\text{Company's score per year} = \frac{0 * A + 1 * B + 2 * C + 3 * D}{51 * 3} * 100$$

where:

A – the number of full non-compliance or not applicable responses

B - the number of non-compliance, but explained responses

C - the number of partial compliance responses

D - the number of full compliance responses

51 - the total number of questions/recommendations



### **3 DEVELOPING THE ANALYSIS AND COMMENTING THE OBTAINED RESULTS**

The Bucharest Stock Exchange, through the Corporate Governance Code which is applied since 2008, lays down principles and/or recommendations which are not mandatory, but listed companies must comply with them or explain why they are not complying with some of their provisions. For this reason, from 2010, listed companies must to prepare the “Comply or Explain” Statement that has a mandatory and public application, which explains the areas of compliance as well as the reasons for non-compliance.

Table 1 Financial companies score

Symb.	Companies	2009	2010				Total 2010	2011				Total 2011	2012				Total 2012	2013				Total 2013
			0	1	2	3	%	0	1	2	3	%	0	1	2	3	%	0	1	2	3	%
BCC	BANCA COMERCIALA CARPATIC A S.A.	N/A	-	1	1	49	<b>98.04%</b>	-	1	-	50	<b>98.69%</b>	-	1	-	50	<b>98.69%</b>	-	-	-	51	<b>100.00%</b>
TLV	BANCA TRANSILVANIA S.A.	N/A	the information cannot be found on the website					10	3	-	38	<b>76.47%</b>	10	3	-	38	<b>76.47%</b>	6	3	-	42	<b>84.31%</b>
BRD	BRD GROUPE SOCIETE GENERALE S.A.	N/A	-	9	-	42	<b>88.24%</b>	-	5	-	46	<b>93.46%</b>	-	5	-	46	<b>93.46%</b>	-	5	-	46	<b>93.46%</b>
FP	FONDUL PROPRIETATEA	N/A	the information cannot be found on the website					-	1	1	49	<b>98.04%</b>	-	1	1	49	<b>98.04%</b>	-	1	1	49	<b>98.04%</b>
BRK	S.S.I.F. BROKER S.A.	N/A	the information cannot be found on the website					8	10	-	33	<b>71.24%</b>	6	11	-	34	<b>73.86%</b>	5	13	-	33	<b>73.20%</b>
SIF1	SIF BANAT CRISANA S.A.	N/A	-	3	-	48	<b>96.08%</b>	the information cannot be found on the website					-	3	-	48	<b>96.08%</b>	-	3	-	48	<b>96.08%</b>
SIF2	SIF	N/A	-	4	-	47	<b>94.77%</b>	-	4	-	47	<b>94.77%</b>	-	4	-	47	<b>94.77%</b>	-	1	-	50	<b>98.69%</b>

	MOLDOVA S.A.																						
SIF4	SIF MUNTENIA S.A.	N/A	-	6	1	44	<b>91.50%</b>	-	6	1	44	<b>91.50%</b>	-	6	1	44	<b>91.50%</b>	-	6	-	45	<b>92.16%</b>	
SIF5	SIF OLTENIA S.A.	N/A	-	12	-	39	<b>84.31%</b>	-	6	-	45	<b>92.16%</b>	-	6	-	45	<b>92.16%</b>	-	9	-	42	<b>88.24%</b>	
SIF3	SIF TRANSILVANIA S.A.	N/A	-	6	-	45	<b>92.16%</b>	-	6	-	45	<b>92.16%</b>	-	5	-	46	<b>93.46%</b>	-	4	-	47	<b>94.77%</b>	

(Source: authors' computation)

Within Table 1 we presented the codifications for the financial companies listed in the premium (first tier) category at Bucharest Stock Exchange. The analysis was made for the period 2009–2013, in order to see the evolution of disclosure on corporate governance principles of these entities before and after the mandatory application of “Comply and Explain” Statement for the listed entities (2010). We can observe that in 2009 no entity presented in a voluntary way the statement. From 2010, after the mandatory application, we found official information (on the Bucharest Stock Exchange or entities’ websites) only for 7 out of 10 Romanian financial listed entities.

In 2014, the only financial entity that is fully compliant with all 19 principles/recommendations from BSE Corporate Governance Code is Banca Comerciala Carpatica S.A. The only non-compliance explained for this company, in the first 3 years from mandatory adoption, was the non-disclosure of information in English. Since 2013 this company discloses periodical and permanently information in this international language. The lowest compliance with the principles we can observe at the company S.S.I.F. Broker S.A. which has obtained only 73.20% for 2013’s declaration based on the presented codification. The above mentioned company and Banca Transilvania S.A. are the only two financial companies that gave negative answers on “Comply or Explain” Statements that were not explained, as this declaration require. This type of answers has a zero scoring in our analysis.

We can see that the evolution of most companies contained in Table 1 is going in a good direction, that is to present and take care of the recommendations made by BSE. For example, SIF Muntenia S.A. has improved the remuneration policy (P10-R21-please see the Appendix 1), BRD - Groupe Societe Generale S.A has drawn up from 2011 a Corporate Governance Regulation which describes the main aspects of the corporate governance principles (corporate governance structures, positions, competences and responsibilities of the Supervisory Board and of the Executive Board) and posted it on the company’s website (P1-R1, R2), and from 2013 established a Nomination Committee (P10).

SIF Oltenia S.A. presented a full compliance on its “Comply or Explain” Statements from years 2010, 2011 and 2012 in what concerns the question “*Does the Supervisory Board or the Audit committee, as the case may be, assess on a regular basis the efficiency of financial reporting, internal control and the risk management system implemented by the Issuer?*” (P12, P13-R28, www.sifolt.ro) and then in 2013 specify that Audit committee did not prepared and did not submitted analysis documents to Supervisory Board. Based on 19 principles that the issuer is managed in a two-tier system, only two companies (Banca Comerciala Carpatica S.A, SIF Transilvania S.A.) complied this recommendation. Two-tier system (German or Austrian Model) is implemented to improve corporate governance and is based on two different management structures: Supervisory Board (non-executive members) and Executive Board, compared to one tier board (UK or USA Model) where we have only a Board containing executive and non-executive members.

In order to show the evolution of compliance with BSE Corporate Governance Code we present the following Figure 1:

Figure 1 Evolution of compliance score for listed companies



(Source: authors' computation)

For three companies (BCC, FP, BRK) we could not find the “Comply or Explain” Statement for years 2010, and for the company SIF Banat Crisana S.A. (SIF1) the Statement from 2011 was not found.

Observing this figure we can notice that there are three types of company evolution based on compliance with corporate governance code: (i) the increasing score meaning that the compliance with principles increased yearly; (ii) the stagnation score meaning that company presented the same compliance within analysed period; (iii) the decreasing score meaning the company changed the application of corporate governance principles and presented a lower compliance.

In the first category we can include the majority of the companies: Banca Comerciala Carpatica S.A.; Banca Transilvania S.A.; BRD-Groupe Societe General S.A. that have an increasing score in year 2011, then it remains at the same level; SIF Moldova S.A.; SIF Muntenia S.A.; SIF Transilvania S.A.

We can observe a stagnation score that was obtained based on our calculation, in the cases of Fondul Proprietatea (98.04%) and SIF Banat Crisana S.A. companies (96, 08%). These two companies were managed in a first tier board and have obtained a good score along the analysis period. These companies conduct their corporate governance based on BSE Corporate Governance Code, or have a plausible explanation for non-compliance.

In the third category we have the following companies: SIF Oltenia S.A. and SSIF Broker S.A. In case of the first company, after presenting in 2011 and 2012 a positive answer (score-3) at the question “*In the course of its activity, is the Supervisory Board supported by any consultative commissions/committees nominated by the Supervisory Board, which deal with the analysis of some specific subjects in order to counsel the Supervisory Board on such topics?*” (P8-R15, please see Appendix 1, [www.sifolt.ro](http://www.sifolt.ro)) in 2013, the answer provided was “No”, with explanation (score-1) that until now certain topics have not been selected for analyse. Also the answer to the principle P11-R21 has been changed from “Yes” in 2010 to “No” with the explanation that the remuneration



policy was established in General Meetings of Shareholders (“GMS”) and the number of independent Supervisory Board members is insufficient.

Table 2 Non-financial companies score

Symb.	Companies	2009				Total 2009	2010				Total 2010	2011				Total 2011	2012				Total 2012	2013				Total 2013
		0	1	2	3		0	1	2	3		0	1	2	3		0	1	2	3		0	1	2	3	
ATB	ANTIBIOTICE S.A.	N/A					6	2	2	41	<b>84.31%</b>	the information cannot be found on the website					1	-	-	50	<b>98.04%</b>	1	-	-	50	<b>98.04%</b>
BIO	BIOFARM S.A.	N/A					11	3	-	37	<b>74.51%</b>	4	2	-	45	<b>89.54%</b>	2	9	-	40	<b>84.31%</b>	2	9	-	40	<b>84.31%</b>
BVB	BURSA DE VALORI BUCURESTI SA	N/A					the information cannot be found on the website					the information cannot be found on the website					1	16	-	34	<b>77.12%</b>	1	11	-	39	<b>83.66%</b>
TEL	C.N.T.E.E. TRANSELECTRICA		9		4 2	<b>88.24%</b>	-	9	-	42	<b>88.24%</b>	-	9	-	42	<b>88.24%</b>	1	5	-	45	<b>91.50%</b>	1	6	-	44	<b>90.20%</b>
COTE	CONPET SA Ploiesti	N/A					the information cannot be found on the website					the information cannot be found on the website					the information cannot be found on the website					4	2	-	45	<b>89.54%</b>
EL	ELECTRICA SA	N/A					the information cannot be found on the website					the information cannot be found on the website					the information cannot be found on the website					the information cannot be found on the website				
ELMA	ELECTROMAGNETIC A SA BUCURESTI	N/A					the information cannot be found on the website					2	25	-	24	<b>63.40%</b>	6	20	1	24	<b>61.44%</b>	4	17	1	29	<b>69.28%</b>
IMP	IMPACT DEVELOPER & CONTRACTOR S.A.	N/A					the information cannot be found on the website					the information cannot be found on the website					2	6	-	43	<b>88.24%</b>	2	6	-	43	<b>88.24%</b>
SNP	OMV PETROM S.A.	N/A					-	6	-	45	<b>92.16%</b>	-	6	-	45	<b>92.16%</b>	-	5	-	46	<b>93.46%</b>	-	5	-	46	<b>93.46%</b>
SNN	S.N. NUCLEARELECTRIC A S.A.	N/A					the information cannot be found on the website					the information cannot be found on the website					the information cannot be found on the website					-	3	-	48	<b>96.08%</b>
SNG	S.N.G.N. ROMGAZ S.A.	N/A					the information cannot be found on the website					the information cannot be found on the website					the information cannot be found on the website					-	11	-	40	<b>85.62%</b>
TGN	S.N.T.G.N. TRANSGAZ S.A.	N/A					-	5	-	46	<b>93.46%</b>	-	4	-	47	<b>94.77%</b>	-	4	-	47	<b>94.77%</b>	-	4	-	47	<b>94.77%</b>

(Source: authors' computation)

Taking a “snapshot” of Table 2 we can see the codifications for the non-financial companies listed in the premium (first tier) category at Bucharest Stock Exchange. We made this separation between the financial and non-financial companies because the first ones need to apply different regulations and laws, so this aspect may cause differences, if we are referring to the compliance with BSE Corporate Governance Code and the filling of “Comply or Explain” Statement.

We can observe that there is only one company (C.N.T.E.E. Transelectrica) presented this statement before the mandatory request across all the listed ones in the premium category of BSE.

The scores obtained by each company are based on the presented codification and we can notice that many of these companies have in their composition the scoring zero based on our codification. This means that on the “Comply or Explain” Statements are negative answers without explanation, as the Statement required.

For the company Electrica S.A. we cannot find the information (“Comply or Explain” Statements) on the company or Bucharest Stock Exchange websites, therefore this company was excluded from our analysis.

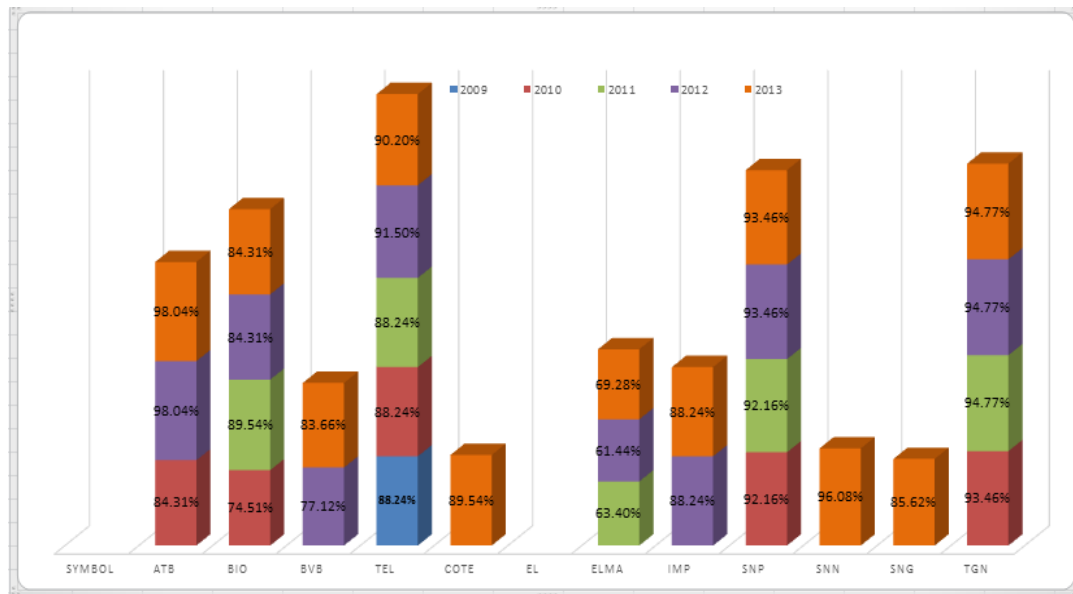
In 2013 Antibiotice S.A. is first in the top of complied listed company with BSE Corporate Governance Code, from the non-financial sector. This company has obtained a score of 98.04% based on the presented codification, even if we do not found the Statement for the financial year 2011. Antibiotice S.A. has develop along studied period some aspects related to corporate governance, such as posted on the issuer website the Statute/Corporate Governance Regulation (mentioning the date of its last update), disclose on its website the information related to the corporate governance policy (P1-R3), ensure a balance between the executive and non-executive members (P6), provide a sufficient number of independent members (P7). On the other hand, at the bottom of the ranking companies we have the company Electromagnetica S.A. Bucuresti with an obtained score of 69.28%.

In some cases, the Statements made over the studied period contained inconsistencies for some principles. For example, presented a positive answer in 2010 and 2011 at the principle P11 –R22 “*Is there a Biofarm S.A. Remuneration Committee made exclusively of nonexecutive members of the Supervisory Board?*”(www.biofarm.ro) and in the next two years (2012, 2013) the response was “No, this Remuneration Committee will be set up on the next period”. Another example for the same company, is on the principle P8 –R15 the answer for the year 2011 was “Yes” and then in the next two years was “No, is not the case”.

Another company that presented inconsistency is Electromagnetica S.A. Bucuresti that in several years has a different answer with the same explanation in “Comply or Explain” Statement. In 2012 the answer at the principle P6 was “No” and in 2013 was “Yes”, with the explanation “the Supervisory Board ensures a balance between executives and non-executives members (five from nine members are non-executives, but none of them matches the criteria to be an independent one)” (www.electromagnetica.ro).

In order to show the evolution of companies’ compliance with BSE Corporate Governance Code we made the following Figure 2:

Figure 2 Evolution of compliance for non-financial companies



(Source: authors' computation)

For some companies we cannot make an evolution analysis of the compliance with BSE Corporate Governance Code because these companies did not post on their websites this declaration. Consequently, for companies Conpet S.A. Ploiesti, SN Nuclearelectrica S.A. and SNGN Romgaz S.A. we found only the data for year 2013.

Taking into account the three types of company evolution presented before, we can observed in the Figure no. 2 that only a company (Impact Developer & Contractor S.A.) presented the stagnation score of 88.24% for two years. Also we introduced in this category the company SNTGN Transgaz S.A. that presenting a score of 94.77% for three years. The rest of the non-financial companies along studied period had a fluctuation in adopting and compliance with the governance code.

## CONCLUSIONS

We assume in our study the fact that these statements are made correctly, according to the Corporate Governance Code, Constitutive Act and other important statements the companies. We conduct this analysis of “Comply or Explain” Statement based on the assumptions that “compliance by adoption” of BSE Corporate Governance codes principles/recommendation is superior to “non-compliance by explanation” or suggest that any action without adoption of principles/recommendation is “noncompliance.”

From our analysis we excluded a non-financial company (Electrica S.A.) because we cannot found data (“Comply or Explain” Statement) in order to develop the analysis for the studied period of 2009-2013.

We made a distinction between financial and non-financial companies because the first ones have different regulations. Financial companies present a higher level of disclosure financial and non-financial information and are more compliant with the BSE Corporate Governance Code than non-financial companies.

In order to better explain our analysis we presented three types of company evolution based on compliance with corporate governance code and place the analysis companies in the following evolution segments: the increasing score - means that the compliance with principles increased yearly; the stagnation score – this companies presented the same compliance on the analysis period; the decreasing score- means that companies changed their application of corporate governance principles and presented a lower compliance with principles/recommendations.

Concluding we have to point two remarks regarding this analysis: firstly, we found that only one company from the final sample (Banca Comerciala Carpatica S.A.) is fully compliant with all 19 principles/recommendations from BSE Corporate Governance Code and secondly, also only one company (C.N.T.E.E. Transelectrica) presented this statement before the mandatory request across all the listed ones in the premium category of BSE became effective.

Most of the observed companies made a step forward in what concerns corporate governance principles and over the study period they disclosed more information on their statements. On the other hand, we found cases where the statements made over the studied period contained inconsistencies (Biofarm S.A., Electromagnetica S.A. Bucuresti) for some principles and some companies had fluctuation along the analysed period in adopting and complied voluntary with BSC Corporate Governance Code.

The contemporary crisis reveals that the informative quality of explanations derived from the corporate governance code's recommendation and for many countries there is insufficient monitoring of the application of these codes (Nedelchev, 2013, p. 79).

The implementation of corporate governance rules ensures transparent decision-making, based on clear rules and objectives, and increases shareholders confidence in the company. Therefore, the degree of compliance with corporate governance principles has an important role in a company's life.

### **Acknowledgement**

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## APPENDIX 1 – Model of “Comply or Explain” Statement

Principle/ Recommendation		Question
P19		Is the issuer managed in a two tier system?
P1	R1	Has the Issuer drawn up a Statute/Corporate Governance Regulation which describes the main aspects of the corporate governance principles?
		Is the Statute/Corporate Governance Regulation (mentioning the date of its last update) posted on the website of the Issuer?
	R2	In the Statute/Corporate Governance Regulation, are there defined corporate governance structures, positions, competences and responsibilities of the Supervisory Board and of the Executive Board?
	R3	Has the Annual Report of the Issuer a chapter referring to corporate governance, which describes all the relevant events related to corporate governance registered in the previous financial year?
		Does the Issuer disclose on its website the information related to the following aspects of its corporate governance: a) a description of Issuer’s corporate governance structures?
		b) the updated Articles of Association?
		c) the internal regulation governing the functioning /its essential aspects for each special commission/ specialized committee?
		d) the “Comply or Explain” Statement?
		e) the list of the Supervisory Board members specifying which members are independent, of the Executive Board and of the special commissions/committees?
	f) a brief version of the CV of each Supervisory Board and Executive Board member?	
P2		Does the Issuer respect the rights of the holders of the financial instruments issued by the Issuer, ensuring equal treatment for them while also submitting any change of the granted rights for approval by the special meetings of such holders?
P3	R4	Does the Issuer publish in a special section of its website the details of the holding of the General Meetings of Shareholders (“GMS”): a) the GMS convening notice?
		b) the materials/documents relating to the items on the agenda, as well as any other information about the items on the agenda?
		c) the templates of the special power of attorney?
	R6	Has the Issuer drawn up and submitted for the GMS approval procedures for an efficient and methodical holding of the GMS according to procedure, however without prejudice to the right of any shareholder to freely express their opinion on the topics subject to the debates?
	R8	Does the Issuer disclose in a special section of its website the shareholders’ rights as well as the rules and procedures for the attendance at GMS?
		Does the Issuer provide the information in due time (immediately after the GMS) to all shareholders through the special section on the Issuer’s website:

		a) the resolutions passed by GMS?
		b) the detailed results of voting?
		Does the Issuer disseminate through the special section of the Issuer's website, which is easily identifiable and accessible:
		a) ad-hoc reports/official statements?
		b) the financial calendar, the annual, quarterly and half-yearly reports?
	R9	Has the Issuer set-up a special department or has appointed a person dedicated to the relation with investors?
P4,P5	R10	Does the Supervisory Board meet at least once a quarter for supervising the activity of the Issuer?
	R12	Has the Issuer a set of rules referring to the conduct and the reporting obligations relating to the trading of the shares or of other financial instruments issued by the Issuer (" <b>issuer securities</b> ") made on their account by the members of the Executive Board and other related natural persons?
		Are the trades with the issuer's securities made by the members of Supervisory Board, Executive Board or any other insiders on their own account disclosed via the Issuer's website, according to applicable rules?
P6		Does the structure of the corporate bodies of the Issuer ensure a balance between the executive and non-executive members (and especially independent non-executive members) so that the decision-making is not to be dominated by a single person or a group of persons?
P7		Does the structure of the Supervisory Board provide a sufficient number of independent members?
P8	R15	In the course of its activity, is the Supervisory Board supported by any consultative commissions/committees nominated by the Supervisory Board, which deal with the analysis of some specific subjects in order to counsel the Supervisory Board on such topics?
		Do the consultative commissions/committees submit activity reports to the Supervisory Board on the specific subjects assigned to them?
	R16	For the assessment of the independence of their members, does the Supervisory Board use the assessment criteria listed in Recommendation 16?
	R17	Do Executive Board members permanently improve their knowledge through training/information in the corporate governance field?
P9		Is the appointment of the Supervisory Board members based on a transparent procedure (objective criteria regarding personal/professional qualifications etc.)?
P10		Is there a Nomination Committee within the Issuer set-up?
P11	R21	Does the Supervisory Board assess the necessity to have a Remuneration Committee/remuneration policy for the Supervisory Board and Executive Board members at least once a year?
		Has the remuneration policy been approved by the GMS?
	R22	Is there a Remuneration Committee made exclusively of nonexecutive members of the Supervisory Board?

	R24	Is the remuneration policy of the Issuer mentioned in the Statute/Corporate Governance Regulation?
P12, P13	R25	Does the Issuer disclose the information subject of the reporting requirements in English: a) periodical information (regular providing information)?
		b) permanent information (continuous providing information)?
		Does the Issuer prepare and make public the financial report according to the IFRS standards?
	R26	Does the Issuer organize, at least once a year, meetings with the financial analysts, brokers, rating agencies and other market specialists with the view to presenting the financial elements relevant for the investment decision?
	R27	Is there an Audit Committee within the Issuer?
	R28	Does the Supervisory Board or the Audit Committee, as the case may be, assess on a regular basis the efficiency of financial reporting, internal control and the risk management system implemented by the Issuer?
	R29	Is the Audit Committee comprised exclusively of nonexecutive members of the Supervisory Board and is it comprised of a sufficient number of independent members of the Supervisory Board?
	R30	Does the Audit Committee meet at least twice a year, with the view to draw up and disclose to the shareholders half-yearly and annual financial statements?
	R32	Does the Audit Committee make proposals to the Supervisory Board regarding the selection, the appointment, the re-appointment and the replacement of the financial auditor, as well as the terms and conditions of its remuneration?
P14		Has the Issuer approved a procedure with a view to identifying and to settling any conflicts of interest?
P15	R33	Do the members of the Supervisory Board inform the Supervisory Board on the conflicts of interests as they occur and do they refrain from debates and the vote on such matters, according to relevant legal provisions?
P16	R34/ R35	Has the Issuer approved the specific procedures in order to provide the procedural compliance (criteria to identify the significant impact of transactions, transparency, impartiality, non-competition etc.) with the view to identify the transactions between related parties?
P17	R36	Has the Issuer approved a procedure regarding the internal flow and disclosure to third parties of the documents and information referring to the Issuer, considering especially inside information?
P18	R37/ R38	Does the Issuer carry on activities regarding the Issuer's social and environmental responsibility?

**APPENDIX 2 – Companies' Websites**

<b>Company</b>	<b>Website</b>
BANCA COMERCIALA CARPATICA S.A	<a href="http://www.carpatica.ro">www.carpatica.ro</a>
BANCA TRANSILVANIA S.A	<a href="http://www.bancatransilvania.ro">www.bancatransilvania.ro</a>
BRD - GROUPE SOCIETE GENERALE S.A.	<a href="http://www.brd.ro">www.brd.ro</a>
FONDUL PROPRIETATEA	<a href="http://www.fondulproprietatea.ro">www.fondulproprietatea.ro</a>
S.S.I.F. BROKER S.A.	<a href="http://www.ssifbroker.ro">www.ssifbroker.ro</a>
SIF BANAT CRISANA S.A.	<a href="http://www.sif1.ro">www.sif1.ro</a>
SIF MOLDOVA S.A.	<a href="http://www.sifm.ro">www.sifm.ro</a>
SIF MUNTENIA S.A.	<a href="http://www.sifmuntenia.ro">www.sifmuntenia.ro</a>
SIF OLTENIA S.A.	<a href="http://www.sifolt.ro">www.sifolt.ro</a>
SIF TRANSILVANIA S.A.	<a href="http://www.siftransilvania.ro">www.siftransilvania.ro</a>
ANTIBIOTICE S.A.	<a href="http://www.antibiotice.ro">www.antibiotice.ro</a>
BIOFARM S.A.	<a href="http://www.biofarm.ro">www.biofarm.ro</a>
BURSA DE VALORI BUCURESTI SA	<a href="http://www.bvb.ro">www.bvb.ro</a>
C.N.T.E.E. TRANSELECTRICA	<a href="http://www.transelectrica.ro">www.transelectrica.ro</a>
CONPET SA Ploiesti	<a href="http://www.conpet.ro">www.conpet.ro</a>
ELECTRICA SA	<a href="http://www.electrica.ro">www.electrica.ro</a>
ELECTROMAGNETICA SA BUCURESTI	<a href="http://www.electromagnetica.ro">www.electromagnetica.ro</a>
IMPACT DEVELOPER & CONTRACTOR S.A	<a href="http://www.impactsa.ro">www.impactsa.ro</a>
OMV PETROM S.A.	<a href="http://www.petrom.com">www.petrom.com</a>
S.N. NUCLEARELECTRICA S.A.	<a href="http://www.nuclearelectrica.ro">www.nuclearelectrica.ro</a>
S.N.G.N. ROMGAZ S.A.	<a href="http://www.romgaz.ro">www.romgaz.ro</a>
S.N.T.G.N. TRANSGAZ S.A.	<a href="http://www.transgaz.ro">www.transgaz.ro</a>

## CULTURAL REVERSAL: WHY DOES OBEDIENCE LOSE WITH THE INITIATIVE?

Karel SLINTÁK

### ABSTRACT

*The article deals with the question which management philosophy is better, management philosophy based on culture HOW or management philosophy based on culture WHY. With respect to this article, author used these techniques, namely quantitative research, case methodology and literature analysis. Consequently, from the research, it can be predicted that most companies prefer a management model which inclines more towards planning, organizing and controlling than to leadership. This approach is a part of the traditional management system through which the organizational culture of "HOW" is implemented. The hidden costs of this model are apathetic staff, lost revenues and mainly work-related stress. These factors, which cause a lack of participation in the workplace, similarly lead to paralysis of innovation capabilities of most companies. They negatively affect the overall productivity of the economy and cause considerable social costs. However, there is also alternative management system based on the WHY culture. This management system, which releases initiative, creativity and enthusiasm, was investigated in the Toyota, FAVI and W. L. Gore. Author found out that these companies are able to eliminate the negative consequences of the traditional management model. The key features of this model are trust, freedom and responsibility, all three of which enrich the system with the ability to learn iteratively from one's own mistakes.*

### KEYWORDS

*bureaucracy, freedom, leadership, management innovation, organization culture, performance, responsibility, trust.*

### JEL CLASSIFICATION:

*M12, M14, L25*

### INTRODUCTION

The stimulus for writing this article was a research report by Towers Perrin (2007-2008). The aim of this study was to conduct a survey looking at employee satisfaction in eighteen countries in the world. The researchers succeeded in addressing 90,000 respondents. Subsequently, extremely surprising conclusions arose from the research. Firstly, only one fifth of employees were fully engaged, in the sense that they were willing to fulfil work tasks beyond their duties. Secondly, two-fifths of employees were totally unengaged while committing work tasks. The remaining respondents were included in the category characterized by formal obedience.

The question which arose while reading this report was: what causes such low involvement of people in the workplace? Looking at the prevailing management ideology, where profit is the only or main priority, the answer was offered directly. Companies often deal with an inability to define actual performance and to identify the factors that affect it. Most managers do not realize the connection between involvement and performance. However, there are several studies which clearly demonstrate such a connection (see Towers Perrin 2006, 2007 - 2008; Sisodia, Wolfe and Sheth 2007).

This article will extend the knowledge already revealed in previous studies. Therefore, it will address the question of efficiency and performance and subsequently uncover the management model which is taken as a consequence of the ideology of classical management. Moreover, it will attempt to map the hidden costs that this model involves. It will also propose an alternative model of management and governance that should mean a radical cultural change in the conception of the human in the workplace.

## **1 THEORETICAL BACKGROUND**

There are many authors who deal with the differences between leader and manager. One of the first authors was Zaleznik (1977), who noticed that leaders and managers differ in their concepts. The manager creates processes. The leader modifies them to make work more interesting. The manager restricts freedom, while the leader does the opposite – he gives space to others in an effort to pass on to them a greater part of responsibility. According to Gardner (1990), there are six important differences between manager and leader: 1. Leader thinks in the long-term context, 2. Leader perceives relations in a wider context, 3. Work of the leader is not defined by its function, 4. Leaders focus on vision, values and motivation, 5. Leaders are able to satisfy various stakeholders, 6. Managers are dependent on organizations, organizations are dependent on leaders.

John Mariotti (1998) describes the influence of the leader and the manager on human motivation. People who are controlled, do only what they must do. Leaders are able to get from their colleagues extraordinary results. According to Drucker (1998), true leaders is a man who is able to bring up his successor who will be better than himself. Therefore, we can talk about real leadership only when a leader leaves his organization and this organization continues to prosper.

A fundamental differences between leader and manager were summarized by Warren Bennis (1990). Some of them are listed in the following table.



Table 1 Differences between leader and manager.

<i>Manager</i>	<i>Leader</i>
The manager commands	The leader communicates
The manager administers	The Leader innovates
The manager is a copy	The leader is an original
The manager maintains	The leader develops
The manager focuses on systems and structures	The leader focuses on people.
The manager relies on control	The leader inspires trust
The manager has a short-range view	The leader has a long-range perspective.
The manager asks how and when	The leader asks what and why
The manager has his eye always on the bottom line	The leader has his eye on the horizon.
The manager accepts the status quo	The leader challenges it
The manager is the classic good soldier	The leader is his own person.
The manager does things right	The leader does the right thing.

(Source: own processing according to Bennis, 1990, 1994)

Some authors deal only with the leadership. Burns (1982) described in his book known as *Leadership* two basic approaches to leadership. Companies can apply transactional or transformational leadership. Transactional leadership means to achieve individual (separate) targets. Transformational leadership aims to achieve common goals on the basis of mutual cooperation through shared purpose.

Many authors deal also with the question whether there is a difference between management and leadership. Kotter (1990) defines these disciplines in terms of their task. Management is about managing complexity. It is a response to the emergence of large organizations. It brings order. Leadership is about managing change. It is a response to the new business environment which is characterized by increased competition and greater instability. It is a source of innovation. Pascale, quoted by Johnson (1996), understands management as a tool to exert influence and authority to achieve average results. Leadership is the effort to achieve exceptional results. Some authors, for example, Kotter (2000), Senge (1990), Weathersby (1999), come to the conclusion that management represents control, while leadership means creating a shared vision. These views are summarized by Peters (1994) who builds on the idea of Bennis, Kouzes and Posner on leadership and management. According to this author, an essential element of leadership is to develop a vision and to live with accordance to it.

Views of many authors are part of the theories that describe the management and leadership in a wider context. Selected theories are shown in the following table.

Table 2 Theoretical background on leadership.

Theory	Authors	Description
Humanistic theory	Argyris (1957), Maslow (1965), McGregor (1960)	Human beings have internal and external motivation. The most effective form of motivation is internal motivation. Leadership must eliminate organizational barriers and create a working environment that will give people the freedom to realize their potential in the interest of the organization.
Integrative: transformational, values-based	Bennis (1994), Burns (1982)	To lead and be led is an interactive process of interdependence. Leadership transforms organizations by aligning human beings and creating organizational culture that encourages free expression of ideas and opinions.
Results-based leadership	Nohria, Joyce and Robertson (2003)	The authors examined more than 200 managerial procedures to determine which of them are key to achieving extraordinary results. There are four primary processes: strategy, implementation, culture and structure, and four secondary processes: use to talent, innovation, leadership and fusion.
Cultural and holistic leadership	Senge (1990), Schein (1992), Wheatley (1992)	Leadership is related to the ability of organization to create such environment in which people can really grow as human beings. Mutual alignment releases synergy between individuals, organizations and environments.

(Source: own processing)

Theoretical background concludes an overview of selected authors who understand leadership as a service. It concludes particular Greenleaf, Fraker and Spears (1996) a Frick and Spears (1996). These authors define leadership as a service to other people (employees, customers, community). Qualities of the leader are the ability to listen, empathy and development of the community.

However, the author doesn't want to examine only the question of management and leadership. The aim of this article is to explore these two approaches in the context of management philosophy, namely philosophy HOW and WHY. There are not too much literary sources that would examine various management practices through the prism of these philosophies. The author found only one source which partially describes these two types of management philosophy. Morel (2007) describes two types of companies, HOW companies and WHY companies. We can understand this description as a metaphor for different managerial procedures and practices. In other parts of this work, we shows what these management concepts mean and how are affected by the management and leadership.

## 2 OBJECTIVES AND METHODS

The purpose of this article is to think about ways of management in business organizations. Author will examine two basic approaches to management and their impact on the effectiveness and organizational performance. These two basic approaches will be examined in context of organization culture, respectively management philosophy called as culture how and culture why.

Author will try to find answers to these questions:

1. What is better, to manage or to lead?
2. What does it mean how culture?
3. What are hidden cost of how culture?
4. Is there any alternative to how culture?

The first and second research questions fit into the area of performance measurement and two important discipline of management. In the third question, author discusses about the limits of how culture. The last research question deals with innovations in the management system. The effectiveness of the studied organizational model (called a "HOW" company) will be evaluated according to the performance capacity that companies can achieve by using rare resources (the intellectual and creative abilities of human beings).

### 2.1 Quantitative research

The article was supported by data gathered from quantitative research. Descriptive statistics was used as the method for processing the relevant data. Except it, the statistical correlation in contingency tables were analysed by Pearson statistics. P-value is being compared with standard 5% confidence level. Lower value of tested criteria than confidence level leads to rejection of the null hypothesis. The null statistical hypothesis claims there is no association between variables. Calculations have been performed in Excel. Table 3 shows the details of this research.

Table 3 Characteristics of quantitative research.

<b>Statistical sample:</b>	About 850 organizations were approached; fifty-six completed questionnaires were returned. The frequency of organizations by size: <ul style="list-style-type: none"> <li>• 20 % large enterprises, 43 % medium-sized enterprises, 21 % small enterprises, 16 % microenterprises.</li> <li>• The survey return was 6.6%.</li> </ul>
<b>Characteristics of the respondent:</b>	The respondents were employees at the level of middle and upper management.
<b>Evaluation and form processing:</b>	Data were organized into absolute and relative frequencies. Inductive statistics were not used because of the small size of the statistical sample and the low return of questionnaires.
<b>Data collection techniques:</b>	Interactive questionnaire

(Source: own processing)

In light of the number of addressed respondents, the author attempted to ensure a sufficient representative sample. He estimated the necessary minimal sample size using the following relationship:

$$n = \frac{Z^2 p(1 - p)}{d^2} \quad (1)$$

If we require 90% reliability with a permissible error of 11%, then the minimum number of surveyed respondents is the following:

$$n = \frac{1,645^2 * 0,25}{0,11^2} = 55,90960744 \quad (2)$$

According to the calculation above the minimum number of surveyed respondents for a representative sample is 56. Of the total 850 companies contacted, exactly 56 surveys were returned.

## 2.2 Case methodology

To accomplishment of the current research, it has been used the case methodology. This is done to the main objective of finding and describing selected companies which use alternative management philosophy to the culture how. The author focused on three organizations with specific features of management, namely Toyota, FAVI, and W. L. Gore.

Author has analysed various information sources about these companies. Attention of author was focused on the attitudes of these organizations to the people and their motivation. Based on these attitudes, the author described the management model of these companies and their specific forms of organization.

## 3 DISCUSSION

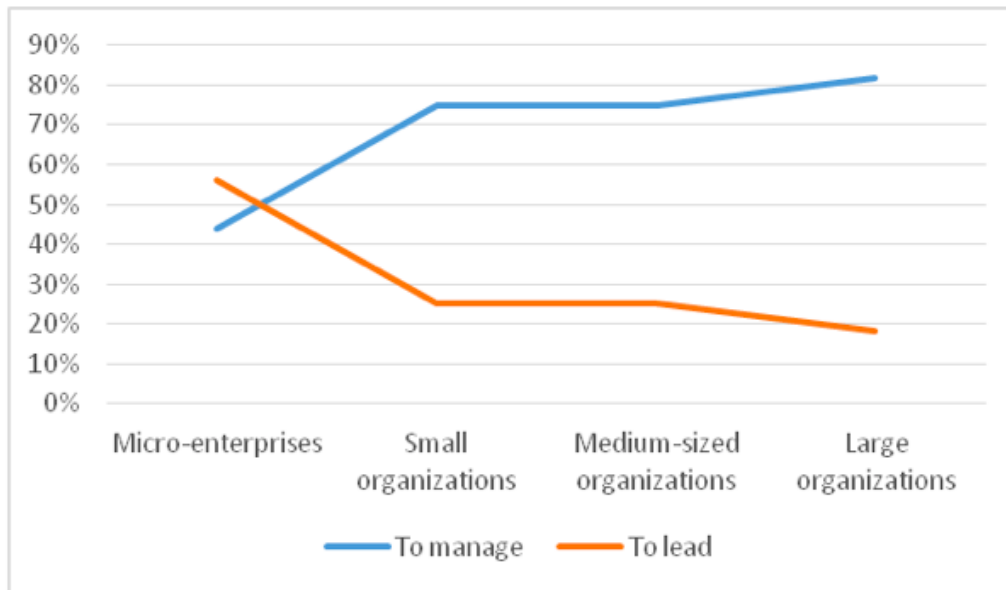
### 3.1 To manage and/or to lead?

Most of today 's companies prefer the term "to manage" than "to lead". As Table 4 shows, the relationship between leadership and management is characterized by the ratio of 1:2 in favour of management. The fact that most companies prefer management is not strongly dependent on the size of the company (as Figure 1 shows, managing and leading only closely approach each other in micro-enterprises). There is not a significant positive relationship between company size and management and leadership (p-value is higher than the confidence level).

Table 4 The attitude toward management and leadership

	Micro-enterprises in %	Small enterprises in %	Medium-sized enterprises in %	Large enterprises in %	p-value
<b>To manage</b>	44%	75%	75%	82%	0,765505984
<b>To lead</b>	56%	25%	25%	18%	0,412114051

(Source: own research)

**Figure 1 Management and leadership in context of company size.**

(Source: own research)

Managing is related to the concept of management as a discipline strictly focused on the results of measurement and thus it is more oriented on the results needed for the evaluation of its own performance. In terms of time, management examines factors that are bounded by a short-term perspective. This characterizes the lower limit of performance. On the other hand, the principle of leadership focuses on areas that are typical for the upper limit of performance. It contributes to the formation of results that fit into a long-term perspective. By using the words of Peter Drucker (2002) and Warren Bennis (1994), “to manage means to do things right, to lead means to do right things.”

The performance of individuals, businesses, and society as a whole is directly affected by these two principles. Covey (2010) explains the importance of these two principles and their application in the context of a story about a group of people placed on a mysterious island. These people want to get to a particular destination. The planners attempt to create a plan and devise a strategy according to an old map. They measure time by a stopwatch and, with the help of organizers and supervisors, they watch over the ordinary workers using machetes in order to hack a way through the vegetation fast enough and in the desired direction. If they work according to the plan, they are rewarded appropriately; however, if not, they are punished accordingly. In this group, there are also people with leadership abilities. One of them climbs the tallest tree, looks around, and shouts: “We are on the wrong island!” The whole group is so busy with operative work that they do not hear him. The man continues to scream and therefore the managers (namely, the planners, organizers, supervisors) silence him since they are too engaged in their management procedures to listen. “Be silent,” they say. “We are still moving forward.” This metaphor does not involve only the diversity of the central principles of management but also touches on the principal foundation of performance, its concept and importance. Therefore, if the concept and meaning of performance change according to the approach to management, we can, according to Kouzes and Posner (2003), see two basic levels of performance in the meaning of the two rooted words, i.e. management and leadership. These two basic levels of performance are namely to manage things (in other words, to achieve the realization of things) and to get to certain point (or to focus).

### 3.2 What does it mean “HOW” Culture?

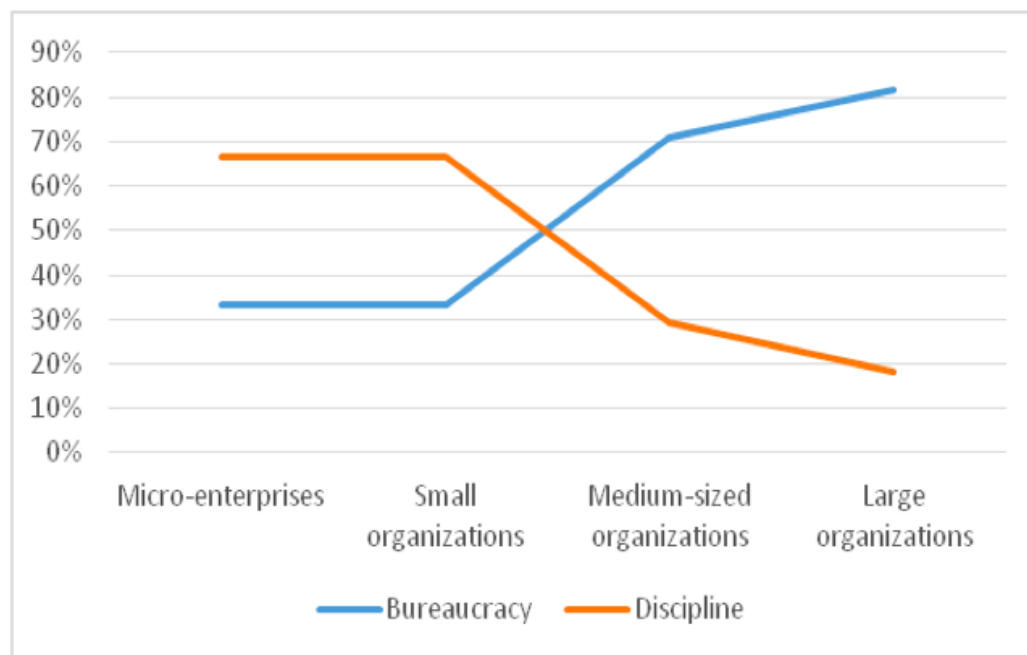
Most large companies are organized on the basis of bureaucracy. This assumption is confirmed by own research, according to which eight out of ten large organizations operate on the basis of bureaucratic structures (see the table below). Analysis of the data also showed that there is not a significant positive relationship between company size and basic forms of organization.

Table 5 The prevailing organizational structure.

	Micro-enterprises in %	Small enterprises in %	Medium-sized enterprises in %	Large enterprises in %	p-value
<b>Bureaucracy</b>	33%	33%	71%	82%	0,273611444
<b>Discipline</b>	67%	67%	29%	18%	0,133871793

(Source: own research)

Figure 2 The prevailing type of organization.



(Source: own research)

In this context, we can talk about “HOW” companies (Morel 2007). A “HOW” company is characterized as a bureaucratic institution in which people have to follow many regulations. The coherence of these companies is ensured by a dense network of commands and controls. The original assumption of this model is based on the unwillingness of people to work. Therefore, the aim of management is to tell people how to do their work (control) and constantly check their activities (manipulate). This model was created at a time when the world gave birth to the first modern business organization, i.e. in the middle of nineteenth century (Drucker 2002). For businesses at that time, this step meant an enormous increase in the productivity of manual workers and an enormous increase in their performance (Drucker 2001, 2002, 2004). Subsequently, this increase in performance economically transformed the whole of western society. According to



Angus Madison (1991), from 1820 to 2001 gross income per capita in western countries increased about twenty times.

However, performance was primarily understood in terms of economic growth. A “HOW” company identifies itself with industrial age. According to this equation, profit is always in first place followed by people (Hamel 2013). Working conditions prevailing in “modern” companies at the height of the industrial revolution were very similar to the working conditions that prevail in manufacturing plants today – and not only in the developing world, with its “sweat shops” and child labour (Carney and Getz, 2013). In both cases, the same management model is implied. In this model, there are people who have the right to dictate (to give precedence) and people who have a duty to listen and obey (to conform).

### 3.3 What are the hidden costs of the “HOW” culture?

Nowadays, the topic of managing for “three percent” is becoming an increasingly discussed problem (Carney and Getz, 2013). These managers should introduce new rules that limit undesirable behaviour in 3% of employees. However, these rules have a subsequent negative effect on the remaining 97% of employees. We cannot be surprised by the traditional manager’s thinking when talking for instance about the problem of theft in the workplace. In this case, the manager’s suggestion might be to introduce measures to search all employees even though the problem is related to only a very small minority. The hidden social costs of this precaution would be the dampening of the initiative and involvement of all employees who were affected by this decision. And the fact that this is not unusual is demonstrated in research by Towers Perrin (2007 - 2008), which revealed that only 21% of employees were truly engaged (see also Hamel 2013). Research by the same company two years later revealed that only about 14% of employees felt engaged in their work (Tower Perrin, 2006; Hamel and Breen 2008). In the case of involvement while meeting corporate goals, the initiative of employees is even weaker, as shown in research by Haris Interactive. S. Covey (2010) makes reference to this research in his book *The 8th Habit* (see the table below).

Table 6 The involvement of workers while meeting targets.

Questionnaire survey (n = 23 000)	Frequency of positive answers
Do employees realize their organizational goals with engaged passion?	9 %

(Source: Covey, 2010)

Low interest among employees indubitably leads to lost income. These kinds of costs arise from low performance capacity – employees simply do not perform extra tasks. The level of commitment among employees does not only affect the internal operations of the company. As illustrated in one study, 73% of customers went to a competitor due to the insufficient engagement of the company or its employees (Carney and Getz, 2013). Thus, when looking at the ability of companies to make a profit through the prism of engagement, we can observe interesting results. According to one survey (Tower Perrin, 2007), it is proven that companies with involved employees can increase their profits in the long-term (in the monitored companies, the average operating profit increased by 3.7% over a period of 3 years). However, the companies with uninvolved employees had reduced profits (in the same period, profits decreased by an average of 2%).

Parkinson’s First Law, which affects all organizations, increases with the size of the organization. As companies increase in size, they not only have to deal with bureaucracy (see Fig.2) but,

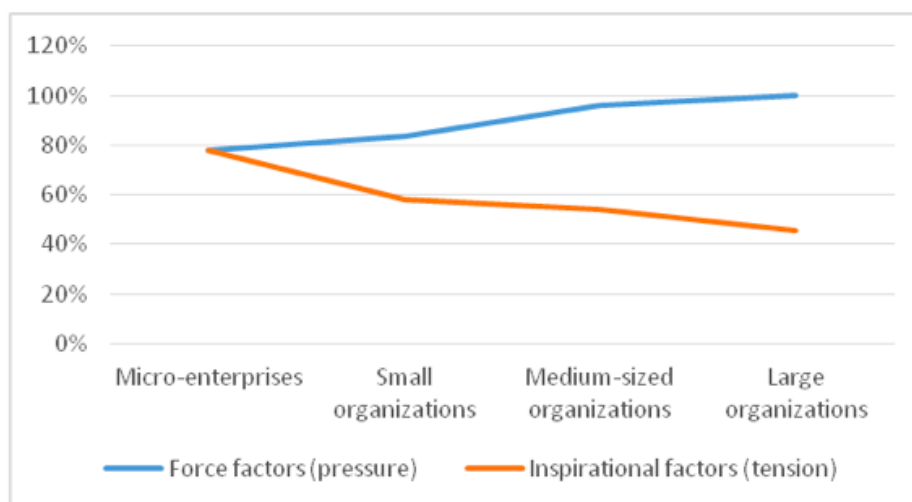
moreover, also need to reflect on two related problems. The first problem is called creeping inefficiency. For a small company, the ratio of managers to other employees is typically 1:10 (9% of employees are managers); one superordinate is in charge of 10 subordinates. For an organization with 10 000 employees, due to Parkinson’s First Law, the number of leading employees and managers may increase up to 1 250 employees and, therefore, the ratio of managers to other employees is reduced to 1:8 (11% of employees are managers). Supposing that the manager’s salary is three times higher than that of his subordinates, it can be quantified that the salaries of the managers represents 38% of the total wage costs. In the first example with small companies, the salaries of the managers represent 27% of total wages.

The second problem is related to the oppressive atmosphere that “HOW” companies create. Our own research shows that, in general, the so-called motivation pressure system predominates in companies, a structure which significantly contributes to a culture of fear and mistrust (see following figure). Motivation pressure system consists of force factors which comprise the survival factor, the fear factor and the money factor. Motivation push system consists of inspirational factors which comprise the enjoyment of work, praise, and self-realization. According to the values of the test criteria, we can state that there are not statistically significant differences between company size and difference factors of motivation.

Table 7 The prevailing motivation in practice.

	Micro-enterprises in %	Small enterprises in %	Medium-sized enterprises in %	Large enterprises in %	p-value
Survival factor	0%	17%	13%	27%	0,442678938
Fear factor	0%	8%	8%	9%	0,701885758
Money factor	67%	83%	88%	91%	0,93600229
Enjoyment of work	22%	17%	21%	9%	0,873679018
Praise	33%	33%	33%	36%	0,999022899
Self-realization	56%	33%	25%	36%	0,298429096

Figure 3 Factors of motivation in practice.



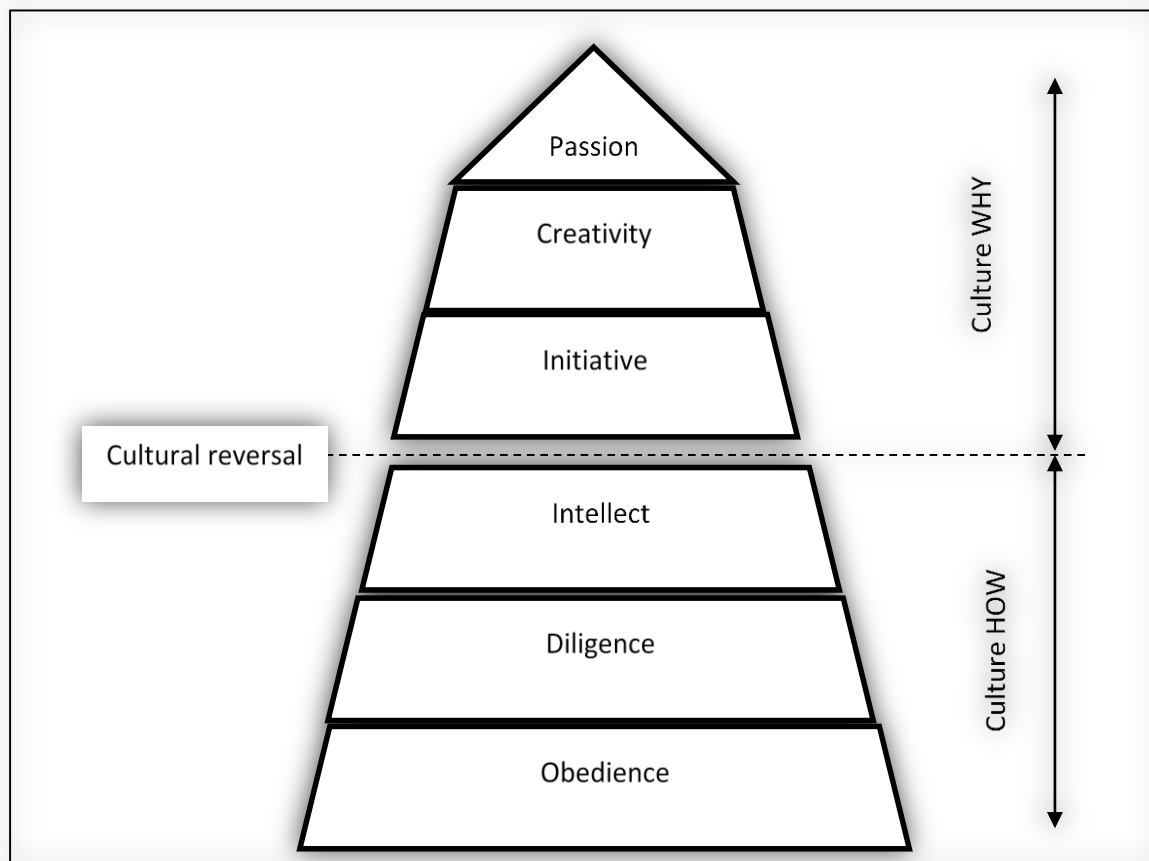
(Source: own research)

The result of this atmosphere is so-called work-related stress (Atkinson 2000; Cartwright and Cooper 1997; Cortina et al. 2001; Wojcik 2001). Stress is activated by so-called stressors that cause a feeling of physical and psychological threat. Stressors can be personal conflicts, unrealistic goals, psychological bullying (being mocked or isolated, for example), a feeling of injustice, or various forms of force motivation (see Neuman, 2004). Stress may also appear in situations in which employees lose control over their work. Work becomes even more stressful when employees do not have sufficient freedom and space to make their own decisions. A sense of hopelessness emerges afterwards. In most cases, growing emotional stress leads to the collapse of goals and corporate vision. However, work-related stress affects not only large organizations. It is an unintended consequence of the “HOW” organizational culture, which can be applied in any organization regardless of its size. This culture prefers obedience before initiative. It appreciates uniformity (and agreement) instead of originality (and disagreement). Animals react to stress by escaping. People react to it simply by avoiding other people or demanding situations that cause stress. Therefore, it can be assumed that apathy at work is influenced by stress. According to The National Institute for Occupational Safety and Health, 40% of US employees are subject to stress at work (comparison with the motivation survey is essential and its results are shown in the table below). In light of this, there exists a legitimate suspicion that work-related stress causes so-called civilization diseases such as headaches, anxiety, stomach cramps, loss of energy, and many others. Therefore, it is not surprising that stress at work is the reason for approximately 80% of visits to general practitioners (Carney and Gets, 2013). What is then the total cost of work-related stress to the economy? In the case of the UK, it is estimated that, due to stress, the economy loses 40 million working days per year and seven billion pounds spent on health care (Handy, 1999). According to Gallup research in 2006, unconcerned behaviour and disengagement caused by stress creates an annual loss of productivity to the US economy amounting to 328 billion dollars.

### **3.4 Is there any alternative to “How” culture**

Work-related stress is the most important source of hidden costs with respect to the traditional management model. Not only companies but also individual states have to deal with it. According to the US Bureau of Labour Statistics, the annual costs associated with work-related stress are 10 000 dollars for each individual employee. The study of work-related stress is closely related to the subjective feeling of the loss of control over a certain situation. So what does it actually mean in terms of the prevailing management system? “HOW” companies apply the technology of traditional management. It is based on the assumption that people are naturally lazy and do not want to work. Therefore, this model uses techniques that are intended to stimulate (activate) human beings to work. The backbones of this model are commands and controls that restrain the feeling of freedom (and responsibility). The “HOW” culture deliberately deprives its employees of the possibility to choose and thus increases the tendency of workers to experience stress. Companies that apply the traditional management model to the imaginary hierarchy of human capabilities, try to put an emphasis on obedience, diligence and intellect (see Fig. 4).

Figure 4 The human capabilities in context of culture Why.



(Source: own processing.)

The hierarchy of human capabilities is similar to Maslow's pyramid of needs. For human beings, higher order needs are combined with greater motivation and satisfaction. For companies, human abilities are assessed according to the benefits of individuals to the whole group (personal performance). In the workplace, people can present themselves by various abilities as indicated in previous figure. When analysing the hierarchy of human capabilities, one question arises and that is whether, in addition to the tradition model, an alternative model of management can coexist. This alternative model is capable of placing human abilities above the level of obedience, diligence and intellect. In this imaginary model, words such as vanity or misappropriation would lose their meaning. Its aim is to humanize the organizational environment. Yet, an important question remains unanswered: are there any companies in the business environment that could become prototypes of companies applying the "WHY" culture?

### Cultural reversal.

#### Example 1: Bureaucracy with a human face

When searching for a prototype of the "WHY" company, we can start with a brief analysis of Toyota. This company, straddling the border of both cultures, has an undoubtedly bureaucratic structure. All processes are planned to the smallest detail. Each employee is governed by predefined working procedures in order to complete a given task in the most efficient way. Consequently, very strong standardization is obvious. The central principle of the company is efficiency, which is ensured by a management technique known as **management through procedures**. All processes must be measured and controlled. What makes this company different from other similarly

bureaucratic companies is its approach to ordinary employees. These ordinary employees are governed by procedures which are not constructed by executives but by the employees themselves. They have only one aim, which is perfection. Everyone is governed by the procedure only until he/she discovers a new and better procedure. Therefore, procedures are not enforced by the head of a certain department. Meeting the goals of procedures is dependent on the employees themselves. In the case of Toyota, effectiveness as a central value is accomplished by **autonomy**. This autonomy is used by employees and teams in order to adjust their working environment. Toyota believes in people's willingness to learn and this is the clear difference in contrast to other bureaucracies. Only through this idea is Toyota able to strengthen the authority of ordinary employees and create a cultural environment that values initiative.

### **Example 2: Management philosophy based on asking question WHY**

An even more interesting example of the transition from the industrial model to a model of the WHY culture can be seen in FAVI. Originally it was a brass foundry which was typical of the industrial era until J.F. Zobrist became its director. After he joined the company he realized that a huge difference exists between the real economy (which includes opportunity costs) and the corporate economy (which works only with the explicit costs). He was inspired by an experience with one of his employees who wanted to change his old gloves for new ones. Zobrist found out that this exchange took place according to a clearly defined procedure. If a worker had damaged gloves, he had to show them to his manager, who would, in turn, furnish the worker with an order form for new gloves. Subsequently, the worker had to visit the store, where, on the basis of a correctly submitted application form, he received new gloves. The entire process of replacing old gloves with new ones took approximately 10 minutes. Zobrist calculated that the cost of operating the machine used by the worker was 100 dollars per hour. From this calculation, he determined that the changing of gloves resulted in *opportunity costs* of 17 dollars per hour. The gloves themselves cost less than 10 dollars!

This "economy" persuaded Zobrist to re-evaluate FAVI's original management philosophy. A new management philosophy was created, based on the idea that there are two types of firms: a "**HOW**" company and a "**WHY**" company. FAVI was an example of a "HOW" company. According to this model, it is usual to tell employees what to do, how long they should work, and when to go to work. Obviously, at FAVI, this behaviour had two consequences. Firstly, employees were evaluated according to all possible scales (number of hours worked, number of units produced, etc.) but not by the scale which is really important (customer satisfaction). Secondly, employees did not have the opportunity to influence their work routine. They were, figuratively speaking, bound by the **chains of bureaucracy** (a change had to be approved by a manager, who had to seek the approval of *his* manager, and so on, *ad absurdum*). By its transition from a "HOW" to a "WHY" company, FAVI had to learn to ask different questions from the ones they had been used to asking for decades. Thousands of HOW questions were replaced only by one question: WHY? The new emerging culture at FAVI no longer wanted to dictate to its employees about how they should do their work. It gave them greater freedom with the proviso that they had to learn to ask the question WHY? In the case of FAVI, asking the question WHY changed the overall focus of the company. As a result, its approach to performance changed, too. By using the question WHY, all corporate efforts began to orientate toward one central point – the customer. This cultural change turned attention away from narrow specialization, strict qualification, and a particular department towards the performance of the whole. And the consequences of this change for the company were radical. The time clock was removed. The new management concept led its employees not to consume time but to produce results. According to the new model, the HR department was closed due to the fact that people were no longer seen as machines but as human beings with specific psychological and physiological needs. Production also underwent several changes. It was restructured into units that formed self-managed teams with approximately 24 employees (an organization that was similar to



the self-organization of workshops applied in the Bat'a Shoe Company). Every production team was responsible for a specific customer and a tailored product. The attempt to change the management model led not only to the invigoration of autonomy in individual workplaces but mostly to the elimination of a formal hierarchy. Each team was able both to choose its own leader and to dismiss its own leader. In general, the transition to the new model has brought significant results. From a long-term perspective, the company has been able to reduce prices to its customers by about three percent per year. Over a period of twenty-five years, it has never experience delays in delivery. It has become the European leader in the production of shift forks for the automotive industry. The size of its market share is reflected in the fact that one half of cars produced in Europe have shift forks produced directly by FAVI. Finally, the company has introduced entirely new products manufactured from brass, which have been exported to China.

### **Example 3: Organizing without formal hierarchy**

W. L. Gore was named one of the “*100 Best Companies to Work For*” in the US by FORTUNE magazine. In addition, another magazine know as *Fast Company* magazine named Gora one of the most innovative companies in the world. This company focused on the production of more than 1,000 products in four divisions (electronics, textiles, consumer products, medical products) certainly attracts attention. It employs about 10,000 associates around the world. It was founded in 1958 by Wilbert (Bill) L. Gore. This chemical engineer left his employer, DuPont, to set up a new company that will be built on a unique organizational principles applied in the DuPont laboratories. Based on work experience from DuPont, Bill Gore have defined three important organizational principles on which he wanted to build his own company. First of all, people achieve the best results when are organized in relatively **small groups**. Secondly, these small teams mustn't be organized on the basis of the hierarchy. It means that team members must **be equal**. Only then they will identify with team goals and fully engage. Thirdly, the success of the projects is bound to the two important principles, **cooperation and freedom**. If people do not have the opportunity to choose what they want to do, they will not be motivated to achieve the best results.

Due to the nature of the company's founder, the organizational culture was influenced by Socratic Method, i.e. rather asking the questions than just giving the right answers. Thanks to this, communication was imbued with dialogue. Gradually, people working in this company has changed the terminology describing the reality of their company. In W. L. Gore, there are no employees. There are the associates. There are no job positions. There are the work commitments. There are no managers. There are the leaders. Leading position arises from the natural hierarchy which is given by the so-called a **goblet of trustworthiness** (i.e. the ability to meet the commitments) and a **level of competence** (knowledge and skills that are used in favour of others).

A typical feature of Gore's culture is also self-discipline. This cultural element replaces to a large extent the traditional management based on the commands and controls. Management model takes on the character of self-management. Each worker becomes a boss himself. The culture of W. L. Gore does not value obedience. This cultural element replaces to a large extent the traditional management based on the commands and controls. Management model takes on the character of self-management. Each worker becomes a boss himself. The culture of Gore does not value obedience. Conversely, the work environment encourages personal initiative and willingness to take risks. This willingness is reflected special management approach called leading to mistakes. The mistakes are not understood as a failure of the individuals, rather it is a source of growth and learning.

Nowadays we can see specific management model in this company which differs significantly from prevailing managerial practices. Gore doesn't work as a hierarchy where are decisions directed from top to bottom. It works as a **lattice or network structure** in which people can cooperate with anyone within the organization to get what they need to do their work. There are no job functions



which would restrict the thinking and acting of workers. There are even no employees as was said previously. All the people working in this company are the associates (in other words partners). Each associate is co-owner of this company. W. L. Gore does not operate on the basis of subordination. This unique feature of Gore's management philosophy reflects **the commitment and passion**. Each associate commits to the work he **wants to do**. Associates discuss their tasks and duties with their colleagues. Work tasks can't be assigned to anyone, tasks can only be accepted in the form of a personal commitment. The company policy is: *All harnesses are personal commitments*. But it isn't anarchy. At the point when the associate commits to something (element of freedom), others expect from him (her) clear results (element of responsibility). In this management model, the freedom (the right to decide) connects with responsibility (the commitment to achieve results). And finally, W. L. Gore has no bosses. It has only leaders who are not appointed by top management, but rather their colleagues. Tribal leader becomes the person who is able to realize the challenging tasks and build efficient teams. It means that you will become the leader in Gore if others follow you.

Values and principles of W. L. Gore, confidence, freedom, responsibility, decency and waterline, created a work environment that releases the hidden human abilities which are initiative, creativity and passion. Due to these abilities, W. L. Gore achieves impressive innovation performance without planning. A number of innovations were born by a lucky coincidence, such as guitar string Elixir or Gore-Tex material. The dynamics of innovation drives free time at work. Each associate has a half-day off during the week. The working environment due to the initiative, creativity and passion resembles a marketplace of ideas in which proponents of new ideas have been competing for time of the best workers, and where workers are eager to join the most interesting projects. No surprise, therefore, that Gore enjoys excellent economic results and profit throughout its existence.

As evidently demonstrated by the experience of Toyota, FAVI and W. L. Gore, it is possible to create alternative management models in which the culture encourages initiative, creativity and passion in each employee. People engaged in these companies work in favour of the profit of their company beyond their work duties. This is so because these companies recognize the huge potential that is hidden in people. The cultural feature of this model is the belief that people together know more than the smartest person among them. And what is the purpose of this model? To manage as little as possible – in other words, to allow people to learn from their own mistakes.

#### 4 CONCLUSION

The most serious consequences of the traditional "HOW" management model are the paralyzing of involvement, the loss of income, and work-related stress. These hidden costs are caused by one factor, namely the lack of employee involvement in the decision-making structures of organizations. "HOW" companies do not trust their own employees and are not willing to pass a large proportion of "management" responsibilities onto their shoulders. Consequently, this causes the suppression of the intellectual potential of companies. Therefore, most companies achieve low performance capacity. An alternative to this management model is a management system based on the "WHY" culture. In the Brazilian company SEMCO, this procedure is called participative management (Semler 2011). The principal value espoused by companies that begin to apply this model is **freedom (and responsibility)**. In these companies, bureaucracy is replaced by a culture of discipline. Employees in this culture are encouraged to experiment (examples of companies with such a culture are FAVI, W. L. Gore) and to build working relationships based on personal commitments. This latter feature is evident in companies such as W. L. Gore or also Morning Star. As demonstrated in several research projects (e.g. see Collins, 2008), the difference between good and great companies is related to the organizational ability to balance on the fine edge between order (responsibility) and chaos (freedom). Overall, this means to build a culture based on personal responsibility in which people are given considerable freedom to realize their own ideas. To create a

working environment in which workers are given freedom is not easy. It requires the ability of organizations to build a shared vision, to determine operating principles, and to define core values. Looking further into the business environment, we can see that there exist many interesting companies that could become prototypes of the “WHY” company. Features of why culture can exist in organizations that use innovative management model built on the principles of trust, freedom and responsibility. Some of these characteristics were seen by other authors at the companies, which include Semco, Morning Star, Google, Apple, Whole Foods Market, IDEO, Harley-Davidson or also SOL. Therefore, further research will be focused on the analysis of companies that apply the principles of trust, freedom and responsibility, these being the typical values of such a new and innovative management model.

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## IFRS VERSUS CZ GAAP: INFLUENCE OF CONSTRUCTION CONTRACTS ON FINANCIAL INDICATORS

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### ABSTRACT

*In 2009, 117 countries all over the world allowed to prepare financial statements according to International Financial Reporting Standards (IFRS) including the Czech Republic. Between Czech General Accepted Accounting Principles (CZ GAAP) and IFRS are some differences involving reporting of noncurrent fixed assets, leasing, construction contracts etc. Using different accounting procedure we can get different value of assets and assets are one component that is used to calculate the financial performance indicators. Those indicators are then used by investors to assess the financial performance of companies and the application of IFRS instead of CZ GAAP can lead to distinct presentation of enterprise performance. In this paper we examine the influence of construction contract reporting using IFRS and CZ GAAP on financial indicators. IFRS leads to more stable development during the period when the project is in progress. In the last year when the project is finished the figures of both ratios (ROA and Z-score) are getting worse which is due to the lower percentage of the construction that is built in this year.*

### KEY WORDS

*construction contracts, IFRS, Czech accounting legislation, financial reporting, financial indicators*

### JEL CLASSIFICATION

*F63, M14, M41*

### INTRODUCTION

International Accounting Standards Board (IASB) was established in 1972 in order to unify the accounting practices all around the world. The widest adoption started in 2002 when European Union (EU) directed the use of International Financial Reporting Standards (IFRS) for all companies that are listed on any of the European stock exchanges since 2005. Since 2000 International Financial Reporting Standards (IFRS) are allowed to be implemented into the national accounting legislations for all countries.

When the Czech Republic entered into the EU, one of the conditions was to implement the usage of IFRS for all consolidated financial statements and individual financial statements of listed companies while for tax purposes it is mandatory for all entities to report individual financial

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statements according to CZ GAAP. For the Czech enterprises this obligation means double reporting according to both CZ GAAP and IFRS.

In our research we want to show the influence of construction contracts on individual financial statements according to CZ GAAP and IFRS and the influence on financial indicators.

## **1 REVIEW OF LITERATURE**

### **1.1 Differences between accounting systems**

Each country has its own specifics and national regulation that expressively influence the amount and quality of disclosures. Some of the reasons are reporting traditions and discrepancies in national law requirements. (Barbu, Dumontier, & Feleaga, 2014) Although the process of harmonization has begun in order to compare the financial statements across the countries, some countries prefer IFRS adoption more than the others. One of the reasons is economic network theory and based on this theory, the network effect is needed for IFRS adoption. This effect strength when the business partners come from the countries that use IFRS. (Ramanna & Sletten, 2009) One of the most discussed advantages of the adoption are information costs. Those costs relate to knowledge of accounting standards by accountants, auditors, investors, financial analysts etc. (Márquez-Ramos, 2011) It also makes the work of financial analysts easier and the predictions of the development in such countries are more precise than in case of different accounting systems. (Bae, Tan, & Welker, 2008)

When EU directed the use of IFRS for all entities listed on the European stock exchange and for consolidation purposes, the European countries had to implement IFRS into their national accounting legislation. This means a lot of amendments to accounting law e.g. in case of the Czech Republic from 1 May 2004 when the Czech Republic entered into EU, 22 amendments were issued. (Act No. 563/1991 Coll., on accounting, as amended)

The Czech Republic is affected by tax requirements demanded by Tax Authority (Strouhal & Deari, 2011) while IFRS is primarily dedicated to shareholders decision-making. (Sucher & Jindřichovská, 2004) Due to this, the Czech enterprises that want to prepare financial statements under IFRS have to issue disclosure under both IFRS and CZ GAAP. Between CZ GAAP and IFRS are some differences such as substance over form principle that are used in IFRS while in CZ GAAP the form over substance principle is used, valuation of fixed assets, revenues recognition etc. In this research we compare differences between construction contracts under CZ GAAP and IAS 11 Construction Contracts.

According to IAS 11 the construction contract is defined as a contract specifically negotiated for the construction of an asset or a group of interrelated assets and shall be applied in accounting in the financial statements of contractors.

### **1.2 Financial reporting, performance and indicators**

Financial reporting is an essential source for presenting the financial performance through financial statements. Financial statements should be audited in order to present true and fair view of the financial position so investors could use this information for investment decision-making and not be misled. Measurement of company's performance is important for variety of management decisions. Financial performance is not used only by shareholders but also by other stakeholders such as employees, suppliers, customers or banks for risk assessment and setting of an appropriate interest risk rate. (Pratt, 2010)



Various financial indicators can measure financial performance. Pavláková Dočekalová, Kocmanová, & Koleňák (2015) identified the financial indicators that reflected the company's sustainability according to top management. From 25 indicators the most important are Return on Assets (ROA) and cash flow. Jennings (2003) explains that Earnings before Interest and Taxes (EBIT) was composed because Earnings after Taxes (EAT) presented in financial statements did not reflect financial performance. EBIT is not influenced by taxes, financial or investment activities and therefore it is the appropriate indicator for operating operations assessment.

Focusing on long-term performance it is needed to connect the financial indicators with other company's components such as social responsibility or attitude to environment. Interconnecting all of the inputs (e.g. legal requirements, social comparison with competitors, technology investments, % woman in top management) the long-term financial performance is mainly reflected by Economic Value Added (EVA) and Return on Capital Employed (ROCE). (Epstein & Roy, 2001) Studying 401 financial representatives (financial directors, shareholders, accountants etc.) it has been found that the most important indicator for external users is Earnings per Share (EPS) even more than cash flow. (Graham, Harvey, & Rajgopal, 2005)

There were researched differences between IFRS and US GAAP and their influence on financial indicators. The variation was found in Return on Equity (ROE), inventories turnover and interest coverage ratio. On the other hand no differences were found in liquidity quick ratio. (Seay, 2014) Assessing the financial situation using bankruptcy model Z-score, 20% of studied enterprises disclosed worse total result using IFRS than using CZ GAAP. 80% of the entities did not note the change in total result but there were negative movements between 2% and 35% within the same zone. The most significant differences between partial indicators were noted in total assets. (Kubičková, 2011)

In our research we want to show the influence of construction contracts on individual financial statements according to CZ GAAP and IFRS and the influence on financial indicators.

## 2 METHODOLOGY

### 2.1 Accounting for construction contracts

In CZ GAAP, the contracted amount is booked as receivable in balance sheet (BS) as asset and total expected income is recognized in deferred income in BS as liability. Deferred income is decreased by the invoiced amount that is accounted as income from work in progress (WIP) in profit and loss account (P/L) and obtained cash lowers receivables. When the company pays for the construction in progress the paid amount is booked as WIP that is valued in costs in BS as asset. Expenses related to WIP that are invoiced to the customer are booked in P/L and lower WIP. (Act No. 563/1991 Coll., on accounting, as amended)

*Table 1 CZ GAAP booking*

SITUATION	DEBIT	CREDIT
Contract signed	Receivables	Deferred income
Paid costs for construction by the construction company	WIP	Cash
Expenses that are part of invoice to customer	Expenses related to WIP	WIP
Invoiced amount to customer	Deferred income	Income from WIP
Paid invoice by customer	Cash	Receivables



According to IAS 11 there are two ways of revenues and expenses recognition: the stage of completion method (SoC) that is used when the company can estimate the costs or zero-profit method in case that the company cannot estimate the costs. IFRS requests to book the construction contracts as work in progress that is the same as in CZ GAAP. In this paper we book work in progress according to SoC method because the company is able to set the expected costs reliably. The percentage of completion is calculated as share of actual costs divided by the expected costs for the whole construction (cost to cost method). Using the same percentage the income from work in progress is booked in P/L and the double entry for this transaction is booked in the amount of actual costs as expenses for work in progress and the rest of the amount increases the work in progress account. The receivables are accounted in the same amount as the issued invoice. The issued invoice amount is booked on separate account. (IAS 11 Construction contracts)

Table 2 IFRS booking

SITUATION	DEBIT	CREDIT
Paid costs for construction by the construction company	WIP	Cash
Invoiced amount to customer	Receivables	Amount billed to customers
Paid invoice by customer	Cash	Receivables
Revenues recognition	WIP	Income from WIP
Expenses that are part of invoice to customer	Expenses from WIP	Income from WIP

In Table 1 and Table 2, the double-entry booking for each accounting system is described. This practice is also used in our calculations that are included in the Appendices at the end of this paper.

### 2.1.1 Financial indicators

Based on the literature review above we identified the indicators that influence the shareholder's decision-making process. During our research we focus on two selected indicators and show how the diverse accounting system changes the values of them. From the ratios we chose ROA and Z-score calculated by course of Altman model. The equations are according to (Kislingerová, 2010) as follows.

$$ROA = \frac{EBIT}{Assets} \quad (1)$$

$$Z\text{-score} = 0.717 * \frac{WC}{Assets} + 0.847 * \frac{EAT}{A} + 3.107 * \frac{EBIT}{A} + 0.42 * \frac{Share\ capital}{Liabilities} + 0.998 * \frac{Revenues}{A} \quad (2)$$

When Z-score is higher than 2.9 the company belongs to the prosperity area, when the result is between 1.2 and 2.9 the company belongs to grey area and when the resulting value is below 1.2 the company is endangered by the potential bankruptcy.

### 2.2 Illustrative example

In order to show the influence of construction contracts on individual financial statements after CZ GAAP and IFRS we suppose that the only influenced items are those related to construction contracts and the rest of the financial statements notices no change in figures. For our research we use illustrative example.

The construction company presents the following items in the financial statements:

Table 3 Illustrative example: Financial statements

ASSETS	AMOUNT IN MEUR	EQUITY AND LIABILITIES	AMOUNT IN MEUR
Non-current fixed assets	62	Share capital	120
Receivables	34	Short-term payables	93
Cash	117		

The company concludes the contract for 170 million of EUR (MEUR) that is expected to be finished during following 4 years. The entity expects expenses amounting to MEUR 154. According to the contracts the customer pays for the issued invoices each month in arrears for the first two years and the rest of the payments is paid after completion.

In Year 1 we assume that the costs incurred amount MEUR 42 and there is no change in total expected costs. The company issued invoices amounting to MEUR 38.5 and the customer paid MEUR 35 until the period ends.

In Year 2 the costs incurred during the period are MEUR 49, which is higher than the expectation by MEUR 3. Issued invoices equal to MEUR 42.2 out of which MEUR 38.3 is paid before the end of the year so as the rest of invoices from the previous period.

In Year 3 the costs incurred are MEUR 43, which is below the original expectation. There are no issued invoices but the company obtain MEUR 5, the rest of the invoiced amount.

In Year 4 the costs incurred in the period reach to MEUR 27, which is higher than MEUR 21 that represents the expected costs. The entity issues the rest of the invoices and the whole amount is paid by the customer.

The aim of our research is to show what differences in financial statements are caused by construction contracts under IFRS instead of under CZ GAAP and how it influences the selected financial indicators.

### 3 RESULTS AND DISCUSSION

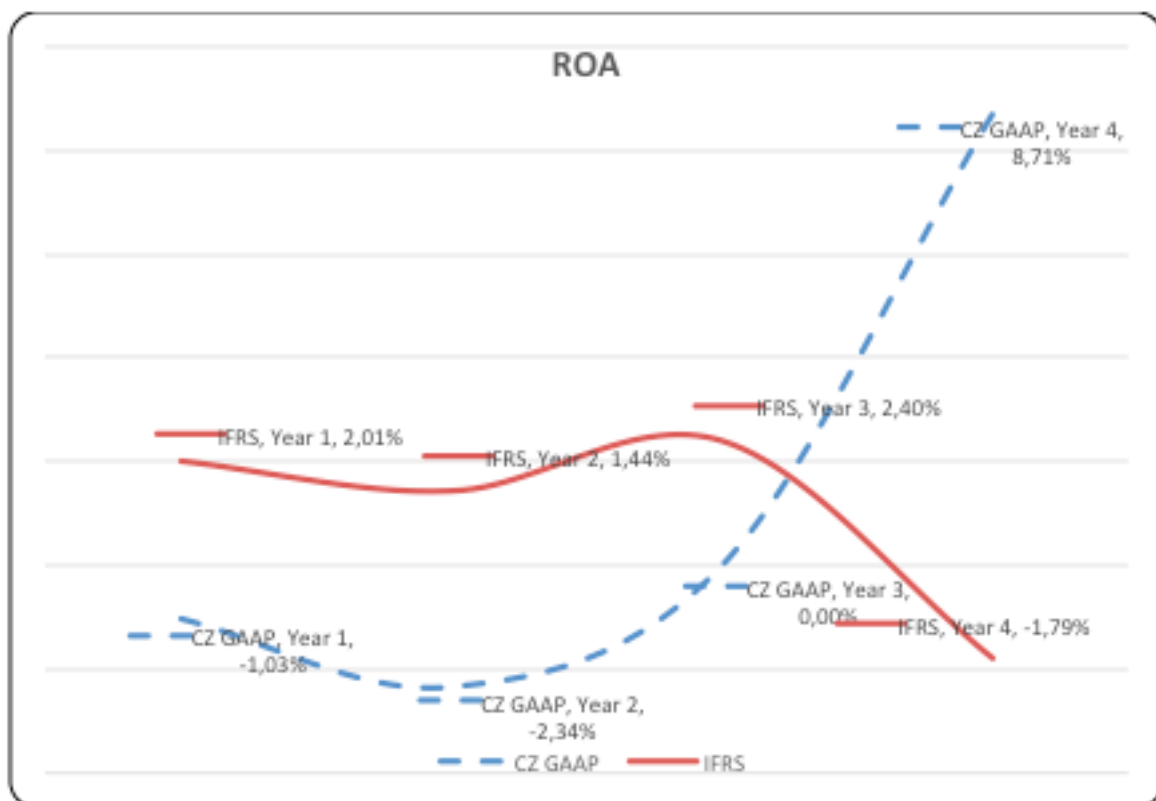
Under IFRS we calculate the revenues and costs pursuant the stage of completion instead of invoiced amount during the period which causes higher revenues owing to the fact that the invoices are issued once a month in arrears and therefore the revenues in CZ GAAP are booked in later periods. (Appendix 1) During Year 1, the costs incurred are booked in the same period which causes the negative profit according to CZ GAAP while IFRS profit is positive. The same situation is in Year 2. In Year 3, there is zero profit under CZ GAAP because there are no issued invoices. Therefore, there are no revenues so as no costs related to those invoices. After IFRS negative profit in Year 4 is caused by the revenues that are lower than in prior years. This is due to the stage of completion because until Year 3 86.45% of the construction was finished while it was built only 13.55% in Year 4.

Using CZ GAAP the total project price is booked as receivable which is then decreased by the repayment of invoiced amount. This causes very high receivables which have declining trend for the whole period except of Year 3. There are paid only invoices from previous periods. Work in

progress exists in Year 3 because there are no issued invoices and no expenses related to WIP. In year 4, there is depression in receivables as the rest of them is paid.

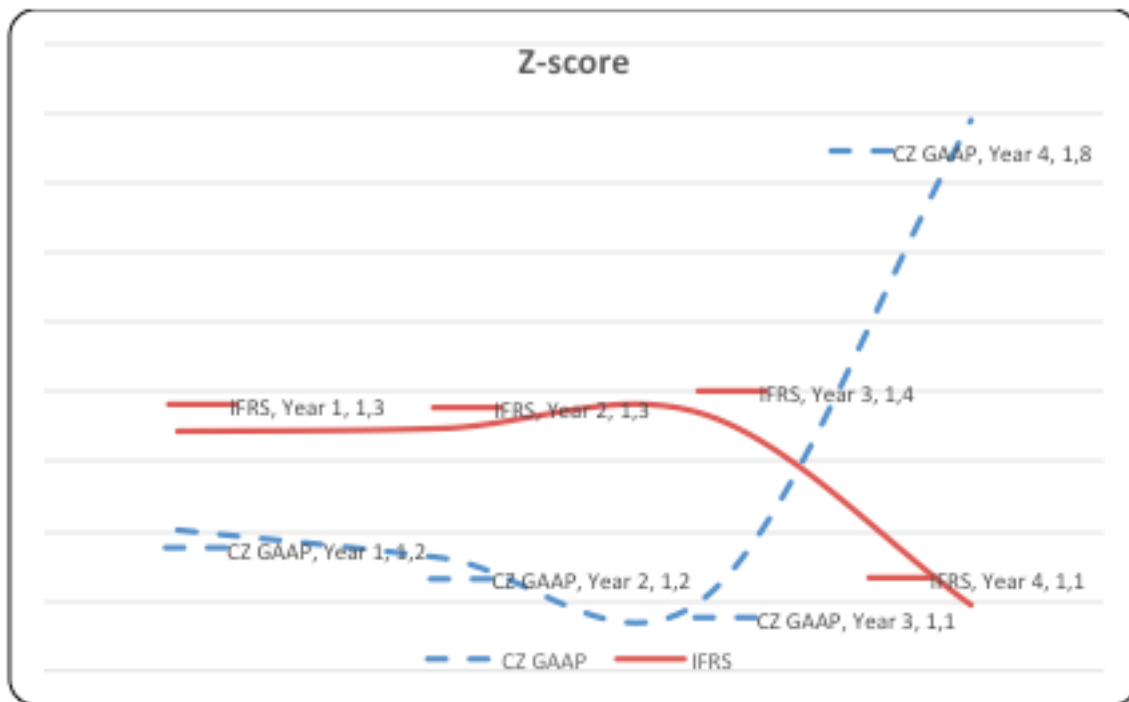
Balance sheet pursuant IFRS shows more stable development with no significant year-to-year movement. This was caused by more even distribution of receivables that are represented by actually issued invoices and not by the contracted price. Comparing IFRS and CZ GAAP BS it can be seen that the total assets are getting closer. In the last year, assets are the same for both accounting systems and they only differ in profit and retained earnings. While IFRS shows negative profit in Year 4 and retained earnings, CZ GAAP presents positive and large profit but shows accumulated loss.

Figure 1 ROA



Return on assets should increase during the period in order to indicate the improving financial performance. As can be seen from Figure 1 IFRS shows stable values during Year 1, Year 2 and Year 3 while in Year 4 there is a significant fall and ROA is negative. This is connected with loss caused by low percentage of construction built in this year. On the contrary, CZ GAAP presents negative performance during the time when the project is in progress. In Year 4, there is a significant increase, which is represented by large profit with the same value of assets as in the case of IFRS.

Figure 2 Z-score



Z-score calculated according to CZ GAAP has in the first three years lower values than under IFRS. In Year 3, the company after CZ GAAP shows value 1.1 which is the area of potential bankruptcy. On the other hand, in Year 4 the value grows to 1.8 which represents grey zone and comparing with Year 3 the entity shows improving development. Pursuant IFRS there is a small increase between Year 1 and Year 3 when the figures are slightly above the line of potential bankruptcy. In Year 4, the development is opposite than in case of CZ GAAP when the numbers drop below this line and the company indicates potential bankruptcy risk.

There are two parts of Z-score that the most influence the values: WC/A and Rev/A. Rev/A has higher wage in the equation and the greater differences are noticeable. This is caused by the fact that IFRS shows more stable revenues during the period. In Year 4, the income declines. CZ GAAP on the contrary recognizes revenues with invoice issuing. In Year 4, the invoice for MCZK 89 is issued and therefore large revenues are recognized. Second factor are more stable assets according to IFRS while CZ GAAP presents greater asset balance. In Year 4, CZ GAAP shows the smallest assets with the highest revenues from all four years.

Assessing the company's performance using Z-score model, there is diverse interpretation of the results. After CZ GAAP we see that during the first three years the enterprise indicates problems with prosperity and there is a risk of potential bankruptcy. But when we check the figures in Year 4 we can state that the entity probably does some positive steps because Z-score raises significantly. According to IFRS the values show worse results because during the first four years the numbers are slightly above the bankruptcy line and in Year 4 the value drops down.

We have to emphasize that presenting worsening development by Z-score model can lead to the opinion that the company will actually have problems in the future and the shareholders could start to sell their shares in order to minimize the loss, which can end in the bankruptcy of the company.

## CONCLUSION

The different interpretation of financial indicators can lead to diverse investment decisions. It is necessary to emphasize that the financial indicators are based on the accounting data and therefore it is important to realize what exactly the differences in the accounting systems are.

In our research we assessed the influence of construction contracts under IFRS and CZ GAAP to the values of two performance indicators (ROA and Z-score model). Overall we can state that IFRS lead to more stable development during the period when the project is in progress. In the last year when the project is finished the figures of both ratios are getting worse which is due to the lower percentage of the construction that is built in this year. On the other hand, CZ GAAP presents fluctuation in the values with negative development but after the project completion both indicators show improved values than in case of IFRS. This is mostly owing to the assets that have increasing trend during the whole period and extremely large profit caused by the fact that invoices are issued in very significant amount. We also identified that booking construction contracts using different accounting system has very high influence on profit distribution between profit for current period and retained earnings. While IFRS shows raising retained earnings and loss for current period, CZ GAAP presents accumulated loss and high profit for current period.

Our finding of Z-score calculation showed the opposite result than (Kubíčková, 2011) during the period when the construction is in progress. On the other hand, we got the same results in the last year of construction when the development was worse after IFRS and the entity was transferred from grey area to the area of potential bankruptcy.

The limitation of the research is that we studied influence of only one project and assumed that there are no other differences between CZ GAAP and IFRS. For future research we are going to focus on the other items in the financial statements that can be variously interpreted using diverse accounting system. The partial researches should lead to assessing the overall influence of presenting the financial indicators under IFRS instead of CZ GAAP.

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**ATTACHEMENT 2****Balance sheet – CZ GAAP**

ASSETS	YEAR 1	YEAR 2	YEAR 3	YEAR 4	CAPITAL	YEAR 1	YEAR 2	YEAR 3	YEAR 4
Long-term assets	62.0	62.0	62.0	62.0	Share capital	120.0	120.0	120.0	120.0
WIP	0.0	0.0	43.0	0.0	Profit	-3.5	-6.8	0.0	19.3
Receivables	169.0	130.7	125.7	34.0	Retained earnings	0.0	-3.5	-10.3	-10.3
Cash	110.0	99.3	61.3	126.0	Short-term payables	93.0	93.0	93.0	93.0
					Deferred income	131.5	89.3	89.3	0.0
Total assets	341.0	292.0	292.0	222.0	Total capital	341.0	292.0	292.0	222.0

**ATTACHEMENT 3****Stage of completion**

	YEAR 1	YEAR 2	YEAR 3	YEAR 4
Stage of completion	27.27%	57.96%	86.45%	100.00%
Increase in stage of completion	-	30.69%	28.49%	13.55%

**ATTACHEMENT 4****Balance sheet – IFRS**

ASSETS	YEAR 1	YEAR 2	YEAR 3	YEAR 4	CAPITAL	YEAR 1	YEAR 2	YEAR 3	YEAR 4
Long-term assets	62.0	62.0	62.0	62.0	Share capital	120.0	120.0	120.0	120.0
Due from customers	7.9	17.9	66.3	0.0	Profit	4.4	3.2	5.4	-4.0
Receivables	37.5	41.3	36.3	34.0	Retained earnings	0.0	4.4	7.5	13.0
Cash	110.0	99.3	61.3	126.0	Short-term payables	93.0	93.0	93.0	93.0
Total assets	217.4	220.5	226.0	222.0	Total capital	217.4	220.5	226.0	222.0

**ATTACHEMENT 5****ROA calculation**

		YEAR 1	YEAR 2	YEAR 3	YEAR 4
EBIT	CZ GAAP	-3.50	-6.83	0.00	19.33
	IFRS	4.36	3.17	5.43	-3.97
Assets	CZ GAAP	341	292	292	222
	IFRS	217	221	226	222

**ATTACHEMENT 6****Z-score calculation**

		YEAR 1	YEAR 2	YEAR 3	YEAR 4
Working Capital (current assets)	CZ GAAP	279	230	230	160
	IFRS	155	159	164	160
Liabilities	CZ GAAP	93	93	93	93
	IFRS	93	93	93	93
Revenues	CZ GAAP	39	42	0	89
	IFRS	46	52	48	23
WC/Assets	CZ GAAP	0.82	0.79	0.79	0.72
	IFRS	0.71	0.72	0.73	0.72
EAT/A	CZ GAAP	-0.01	-0.02	0.00	0.07
	IFRS	0.02	0.01	0.02	-0.01
EBIT/A	CZ GAAP	-0.01	-0.02	0.00	0.09
	IFRS	0.02	0.01	0.02	-0.02
SC/L	CZ GAAP	1.29	1.29	1.29	1.29
	IFRS	1.29	1.29	1.29	1.29
REV/A	CZ GAAP	0.11	0.14	0.00	0.40
	IFRS	0.21	0.24	0.21	0.10
Z-score	CZ GAAP	1.20	1.16	1.11	1.79
	IFRS	1.34	1.35	1.37	1.09

