

ABSTRACT: PATRIMONIAL EVALUATION AND ENHANCEMENT OF THE QUALITY OF ACCOUNTING INFORMATION COMMUNICATED THROUGH FINANCIAL REPORTS

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PhD ABSTRACT

“PATRIMONIAL EVALUATION AND ENHANCEMENT OF THE QUALITY OF ACCOUNTING INFORMATION COMMUNICATED THROUGH FINANCIAL REPORTS”

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In the conditions of market economy frequent changes are taking place as far as the number and the structure of economic entities are regarded. Being in competition, there raises the issue of their comparison, especially when it comes to operations of external increase, of participation of a new partner or shareholder to the social capital, of establishment of the warranty value or of warranties for requested credits, desiderata impossible to achieve in the absence of annual financial reports that offer an accurate global image and a complete image on the entity and on the transactions to which it participates, based on pertinent, relevant accounting information. Consequently, starting from this perspective, we consider that the evaluation of the entities becomes quasi-permanent, given the necessity to obtain an accurate real-to-life image deriving from the effective modalities through which this approach is materialized.

Under these circumstances, the major direction of the present research work was represented by dealing with issues in a coherent, articulate and systemic manner, while criticism determined us to take into account both theoretical and practical aspects, developed alongside with the expression of opinions and personal proposals that contribute to obtaining accurate accounting information regarding the patrimony of the economic entity.

Varied information that focus on the dynamics of economic phenomena whose effects must be known and adjusted have constituted and constitute a major centre of interest for the accounting-financial management of any entity, especially if we take into

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account the entities in the Romanian business environment and, if this opinion refers to a piece of information in general, we consider that it characterizes in the same measure the accounting information.

If we transpose this informational necessity to the level of economic entities in our country, then the complexity of our approach increases, and decisions that must be adopted and conclusions that can be drawn request a rigorous analysis, within the framework of which the way in which are carried out the patrimonial evaluation and the accounting valuation receives an important role.

The main axis of the entire analytical approach was based on the idea that, if we saw evaluation from the single perspective of the evaluator, we would not be able to perceive the net demarcation between accounting valuation and economic valuation.

That is why, appreciated as being sufficient, we proposed ourselves -by the research work entitled “**Patrimonial evaluation and enhancement of the quality of accounting information communicated through financial reports**”, - to bring more clarity to the complex issue that focuses on the evaluative approach, guided by the intensity of debates that it generated in the specialty literature in Romania and abroad, but also by the desire to offer compatible responses with the economic climate dominated by incertitude, by crisis and recession in our country.

The main *objective* of the current research work was meant to render successively and in detail the main aspects that focus on the theoretical fundamentals regarding the evaluation of economic entities, the critical description of the specific evaluation methodology, the concrete manner in which evaluation offers the possibility to obtain accurate accounting information, as well as the valuation of this information through annual financial reports.

Chapter 1 of the study entitled „**Delimitations and theoretical fundamentals regarding evaluation**” begins with a short survey of the significant aspects regarding the definition of patrimonial evaluation from the perspective of obtaining accounting information, taking into account the exigencies concerning the evaluation in the context of application of national and international standards in the domain, as well as its necessity, opportunity and objectives.

Judging through the prism of economic theory, we cannot oversee the fact that, if the value of goods is established in the process of exchange by reporting request to the offer (objective appreciations depending on the cost of production factors), being specific to consumption goods, evaluation is specific to goods generating future incomes, or to entities as a whole, as units generating profit.

The theory of evaluation does not operate with the generic concept of value, but with types of value specific to a certain evaluation aim, determined in certain conditions and explained by valuation standards, elaborated by national and international professional associations.

Consequently, we believe that there is no objective value, since the benefit can be different for each person.

We motivate this assertion by the fact that “value represents a conventional quality of a good, of a property or business that is conventionally attributed as result of calculus or expertise. Value is not a fact, but an opinion.”

Starting from the methodological perspective, a pertinent process of evaluation is

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first interesting for the buyers of unquoted entities, each having its individual motivations and a separate investment philosophy.

As far as the evaluation procedure is regarded, an important aspect is linked to the manner in which the administrators of companies are able to appreciate accurately the ensemble of risks to which the company they “pilot” is exposed and to adopt the suitable measure to decrease the effects of some risks.

The retaining of the accurate value as principle in the process of accounting evaluation supposes, inclusively in our opinion, a series of advantages and disadvantages: it will raise serious problems as far as the evaluation of assets is regarded – the evaluation of assets that are not subject to transaction on an active or efficient market, but can ensure a good knowledge of the entity’s market value.

A current major question reads such as follows: which is, in the current economic context, the most appropriate solution: the balance in historical costs or the balance in historical costs and/or accurate value?

Currently, more and more voices are criticizing the accounting reference system issued by IASB that seems too much connected to the American norms and, moreover, places in the centre of its interests the informational necessities of investors.

We agree with the opinion that we must not ignore the national specificity of each state. It is hard to believe that a thorough harmonization in the accounting domain will lead to harmonization and uniformity in the domain of evaluation, of economic, social, cultural, political life, in the juridical or fiscal domain.

Trying a critical comparative approach, we think that compared to accounting valuation that is tributary to strict rules and principles, accounting reports and especially accounting balance that reflects that state of the patrimony and of past activities, at a given moment, the economic valuation has the role to adjust the patrimony of the entity in order to reflect its capacity to produce future incomes. Unlike accounting valuation, economic valuation reports the evaluated object at market conditions.

Consequently, we consider that economic valuation benefits by flexible methods and rules and is decisively based on the understanding of the evaluator in the use of methods adapted to the specificity of the entity and in the reflection of strengths and weaknesses of the entity in a professional honest unbiased way.

The standards foresee a minimum of requirements that must be abided by the evaluators. If certain circumstances, inclusively the express request on behalf of the client necessitate a deviation from the standards requirements, this deviation must be compulsorily mentioned in the evaluation report.

The issue of entities’ evaluation bears greater importance under the current circumstances when at global level we notice the selling-buying of some entities between parties from different countries. Consequently, we draw the conclusion that it is necessary to adopt the evaluation practices that tend to be standardized, since this allows a homogenous image in the all countries of the world, the international norms and standards of evaluation being eloquent as well as the search and finding of compatibilities between regional institutions.

From an accounting point of view, the sphere of interest is nowadays claiming the emphasis on conceptual and methodological aspects linked to entities in the conditions in which the approach of this issue has been subject to continuous evolution, on the

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background of sustained attempts at finding real solutions for the improvement of accounting treatments abiding by the spirit and letter of IFRS.

Chapter 2, suggestively entitled “**Critical analysis of evaluation methods**” is justified in the structure of the elaborated thesis by the importance of the direct connection that exists between evaluation and accounting information at the level of any entity, following from a critical point of view the way in which the evaluative process fingerprints the entities that act in the uncertain business environment of contemporary Romania.

From the viewpoint of phases and steps of the evaluative approach, we can notice the existence of continuous inter-conditionings between them, especially if we take into account the fact that the essential objective

The adjustment of accounting values of assets and debts of the entity and their bringing up to the market value represents the essence of the approach that is carried out in the case of evaluation on assets basis, known also under the name of patrimonial evaluation or on the basis of costs or the approach by replacement cost.

We argue that the perception of this approach through the modality of estimation of the value of an entity and/or stocks, by the use of methods of estimation of the market value of individual assets of an entity minus the market value of total debts represents a modality of definition that we sustain within our approach, given the synthetic character and the thoroughness of its content.

If we considered entering the **regulation sphere**, we can recall the fact that ANC is determined in accordance with the International Financial Reporting Standards (IAS) and with the Order of the Ministry of Economy and Finances no 1752/2005 for the approval of accounting regulations harmonized with the 4th Directive of the European Economic Community.

For the estimation of the entity's value, International Valuation Standards recommend the use of at least two of three types of approaches. The option for a method or another remains the choice of the evaluator who selects methods used depending on the concrete conditions in which evaluation and advantages/disadvantages presented are carried out.

We further considered opportune to focus on the analysis of rectified net asset, whose main trait is that it concentrates on the size of the capital necessary to reconstitute the net patrimony of the entity, at the level of the real value of its utility. The fundamental feature of the method ANCC which consists in the replacement of the balance - that reflects accounting values essentially influenced by the historical cost – with the economic balance, by which all assets and debts are reflected at their market value, represents its great advantage.

The advantage of economic valuation through ANCC method is that it supposes the grouping of asset elements first on the basis of inventory lists and then on the basis of the balance.

The greatest disadvantage of this method resides in that, even if apparently easy to apply, from a technical point of view it leads to a complex activity because of the diversity of assets that need to be distinctly evaluated. We cannot recommend this method to the specificity of Romanian economy, in disfavor of the method of accounting net asset which, in our opinion, reflects much more accurately the used accounting information.

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In conclusion, we can appreciate that the establishment of the entity's value presents a high degree of difficulty due to the multitude of factors that influence it and to the numerous forms they receive. The value of an entity must not be statically followed since it changes fast, under the influence of the market and of the economic-financial market obtained by it.

In the context of these aspects we considered that a continuation of the research carried out is represented by the presentation and analysis in chapter 3 of the **exigencies regarding the evaluation from the perspective of the enhancement of quality of information communicated by annual financial reports**, understood from the perspective of aiming at the insurance of a continuous convergence between theory and practice in our country with the international reference system, as well as between economic valuation and accounting valuation.

The aspect that achieves the joining of accounting and economic valuation is constituted by the common objective of estimation of the value of economic goods, irrespective of the fact that they pertain to a juridical and physical person, a value expressed in both cases by currency standard.

If we use a certified reality and namely the fact that since the beginning of each evaluation, the main source of information in economic evaluation is represented by accounting documents (justifying, accounting registers, synthesis and reporting documents), then the dependence between the estimate value of goods in economic valuations and the estimate value in accounting valuations is confirmed.

On the other hand, at the same approach also arrives the American Institute of Certified Public Accountants that decreed the role of accounting regarding "the furnishing of quantitative information, of financial nature referring to economic entities and that is going to be used in making economic decisions". These decisions also regard the estimation of the value and of the price with which are reflected patrimonial elements in financial reports and implicitly of the entity's value.

This presentation offers us the possibility of formulation of a conclusion according to which there is a clear similarity between the objectives concerning the information presented in financial reports (in accordance with accounting standards) and those existent in the valuation report (in accordance with valuation standards).

The argument marked regarding the interdependence between accounting valuation and economic valuation is represented by fundamental concepts (the accurate value and the market value) used between the two evaluations.

We cannot give up our critical approach, reason for which between the accounting value and the estimate market value by economic valuation we can emphasize certain differences. Thus, the accounting value reflects the historical costs previously achieved (the past in the case in which we choose the basis treatment), while the market value regards the current period (market value) or future period, by cash flows or incomes that it will cash or achieve.

The desire to establish and demonstrate the dependence of accounting economic valuation determines us to analyze the bidirectional relationship between values of estimate asset elements and presented in financial reports and the values of the same goods resulted from economic valuation, by previously mentioned methods.

Chapter 4 entitled "Evaluation in the conditions of application of IFRS and

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IVS” aims to render economic realities in Romania from the perspective of evaluation, reason for which we appreciated as justified the attempt to join and connect IFRS and IVS.

According to us, Romania would substantially benefit as result of this perception, not only from the perspective of conformation with EU legislation, but also from the perspective of the fact that entities in our country use an acknowledged accounting framework at global level, based on the concept of correct and accurate image, that represents a desideratum for the business community. This context represents a challenge for target entities, for implications for these entities are multiple, of which the most relevant refer to the understanding of the main issues and of the potential impact of these issues, the elimination of the potential deficiencies of financial operations from the perspective of IFRS and IVS, the elaboration of budgets and forecast in accordance with IFRS requirements, the development of communication strategies aimed at preparing the market and the involved parties for the potential impact on the main indicators of performance in accordance with IFRS.

The conversion to IFRS is a fundamental change of generally accepted accounting principles, which means that taking into consideration also IVS is not only necessary but also recommended if we wish to carry out an interdependent analysis of IFRS implementation.

In our opinion, it is important to consider that IVSC provides to the accounting profession recommendations and counseling regarding valuation and aims to coordinate its standards and working programs with accounting programs, to the public interest, and cooperates with international organisms to elaborate and promulgate new standards.

We believe that the adoption of IFRS represented more than a modification of accounting settlements.

The necessity and their opportunity allowed the emergence of a new system of evaluation of performance – a new system of procedures that must be adopted at the level of the entire organization. This will change the working manner and it is likely to impose decisive changes in the domain of strategic and accounting management.

The complex, uncertain and risky environment in which the entity unfolds activity demands evaluations in accounting, but in a special way, the revision of estimations. Criteria used with a view to achieve estimations are far from being objective, and the objective is, inclusively in our opinion, necessary to accounting.

We also consider that it is worth mentioning the fact that for the constitution of premises of a pertinent evaluation, Romanian accounting could not remain passive to the challenges to which it is currently exposed, on international level. It tries to solve its problems by the adoption of solutions proposed by the international accounting norms. The implementation, in the Romanian accounting environment, of a system that functions in a social, political, economic climate, much more different than Romanian reality will not be easy to achieve.

IVS represent the best practice or the accepted practice in evaluation, acknowledged also as Generally Accepted Valuation Principles (GAVP).

We consider as justified appreciating as positive the option that IVS and national standards complete each other and sustain themselves reciprocally. IVSC pleads in favor of the recognition of differences between provisions of International Valuation Standards

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and national standards.

Drawing a conclusion, we remind the context in which value is reported, aspect as important as its basis and accuracy. The final value needs reference to market information, to procedures and reasoning that sustain it.

In the same order of ideas, we must also mention the communication of the result of evaluation which in a logical and persistent manner supposes a methodical approach that helps the user to understand the unfolding of the valuation process and the relevance of its conclusion.

The report must communicate to the reader a clear understanding of opinions expressed by the evaluator and must be typewritten and intelligible for someone who does not have previous knowledge on the evaluated property. The report must demonstrate the clarity, the transparence and the consistency of approach.

The evaluator usually manifests prudence in granting permission to use its evaluation to other aims than he whom it is has been initially destined.

On the other hand, informational valences of evaluation can be emphasized within annual financial reports, approaching issues that concern their valuation with the aim to increase the financial performance of the economic entity, within the framework of chapter 5 suggestively entitled **“Critical study of relating the outputs of the evaluation with information communicated through annual financial reports.”**

Analyzing from the perspective of implications of evaluation on modalities of presentation of assets and debts of the entity, their structure can be studied with the help of two groups of financial installments: structural installments of mobile asset elements and structural installments of fixed asset elements.

If we see things from the perspective of the entity’s evaluation, we are entitled to assert that for the appreciation of the financial equilibrium we must take into account several types of “equalities” and “correlations” between the “necessities” and “possibilities” of the entity, respectively between financial sources and economic means necessary to carry out the activity of exploitation and commercialization on short and long term. In the general state of equilibrium are circumscribed both “equalities” of elements, and “inequalities” with their economic significance.

The existence of cash flows and material flows imposes taking into consideration in the definition of financial equilibrium the elements involved in these flows, by specific indicators of characterization. It results that economic-financial equilibrium of the entity must be understood as an ensemble of correlations that are made up within the process of capital rotation. Maintenance of financial equilibrium represents a permanent objective of financial policy that can be considered as achieved when the financial exercise finishes with positive treasury.

The changes that intervene in the value of balance elements, consequence of their re-evaluation, can lead to the “disarrangement” of correlations mentioned above and in this way to the alteration of financial equilibrium.

In our opinion, the analysis of implications of valuation on the financial equilibrium of the entity, imposes the study of liquidity and solvability installments and of the correlation between the working capital, the need of working capital and net treasury.

Thus, the image of the entity that is communicated through accounting information in the business environment depends on the way valuation is carried out, especially on the

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impact that reevaluation and bringing up-to-date have on the level of influenced balance elements, through the indicators of financial position and financial equilibrium.

We considered appropriate to present at the end of our thesis (Chapter 6) **the specific reports of valuation and recognition of results of this activity**, amongst which we recall those referring to valuation, accounting information and fiscality specific to combinations of entities, as well as to those aiming to clear off entities and to guarantee bank credits, that were considered as reference points within the analysis carried out.

Due to its size, an acquisition can have a major impact on capital shareholders, as compared to another capital investment.

If we consider the impact of accounting valuation on the pertinence of gained information as a result of combination between companies, it is pertinent for us to remind that the analysis and making-decision instruments must be applied prudently, according to the size and complexity of the investment involved. A corporate acquisition can take the form of merger by absorption, as well as the form of a merger by reunion.

In Romania, the legislative reform achieved in the economic-financial domain regarding mergers, division and liquidation of commercial entities reveals only absorption with the liquidation of the absorbed entity and merger with liquidation of entities that reunite to make up a new economic entity, a scanty aspect, according to us, in the conditions in which the merger can receive different forms with distinct peculiarities, inclusively at valuation level.

As far as liquidation of economic entities is regarded, we considered appropriate for our approach to study the steps of the process of degradation of the economic-financial situation of the entity, these being an important criterion for choosing the forecast methods for entities in difficulty and also for strategic orientation.

The financial dimension of the degradation of the entity's situation constitutes, in specialty literature, the fundamental element for the definition of the concept of entity in difficulty.

If we tried a critical analysis of management in an entity in difficulty, from the perspective of the way in which valuation is regarded, we can notice that, irrespective of the exogenous or endogenous causes of degradation of the economic-financial situation of an entity, the difficulty state can be emphasized by the late reaction or slow reaction of the management team to the changes intervened, in the conditions in which decisions are made on the basis of information provided in a wrong or unseasonable way by the valuation carried out.

It is extremely important to carry out not only valuation but also financial-accounting audit for it plays an important role in discovering dysfunctions in the economic-financial activity of the entity on due time.

We consider that the decision of an entity of entering or not bankruptcy should be the result of a detailed analysis of causes that have determined the insolvability state, inclusively of the analysis of the manner in which valuation has contributed to the pertinence, or on the contrary, distortion of obtained results.

In conclusion, we can assert that the establishment of the entity's value presents a high degree of difficulty due to the multitude of factors that influence it and to the diversity of forms they receive. The value of an entity must not be statically followed since it changes fast, under the influence of the market and of the economic-financial

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market obtained by it. Granting a dynamic feature is possible through the correlation of the entity's value with its economic and financial performances.

Finally, we mention that we did not achieve an exhaustive approach of the entire issue afferent to the mentioned topic, but achieving a rigorous examination of opinions of different specialists from our country and from abroad, correlated with legislative provisions, but also with criticism, proposals and our own opinions, and we assert that we carried out a research work by which we bring a plus of clarity to the numerous aspects subject to debates, mainly as far as the contribution of valuation is concerned- contribution of valuation to obtaining annual financial reports capable of offering accounting information based on reality and accuracy.

We can affirm that the current work answers to concrete questions with regards to the need to be informed that is manifested in the Romanian business environment. We have formulated suggestions rigorously motivated as result of the analyses carried out, suggestions destined first to decisional factors that can influence the policy of any entity. By its contents, the used methodology, the critical analysis undergone and the final conclusions, they can represent points of interest both for the academic environment and for the business environment.

Finally, we consider that the above mentioned contain sufficient reasons that justify the following **two general conclusions**:

- *Accurate patrimonial evaluation that insures estimates of values as close as possible to those possible to accept in the case of transactions, is based, amongst other things, on pertinent accounting information and on the professional reasoning of the evaluator that must be independent and un-biased. Thus, valuation does not represent a warranty as far as the credibility of information it offers is regarded.*

- *In their turn, accounting information that is obtained through an accurate valuation receives a plus of quality and significantly contributes to the making of economic decisions adequate to a good management of the patrimony and activity of the entity.*