

University of Security Management in Košice

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**ACCOUNTING
MANAGEMENT DECISION TOOL IN
BUSINESS**

monograph

Košice – 2022

Cover and dust jacket: Ioan PRIGOREANU
Typesetting: Ioan PRIGOREANU

Recommended for publication by the Senate of the University of European Studies of Moldova, minutes no 8 of March 28, 2022

Scientific referees:
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Recommended for publication by the Editorial Board of the University of Security Management in Košice

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Accounting management decision tool in business: monograph / Gabriela IGNAT, Nicu ȘARGU. Košice: Vysoká škola bezpečnostného manažérstva v Košiciach, 2022. – 151 p.

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ISBN 978-80-8185-045-5

Motto: It is absolutely indispensable for a man to be introduced to the elements of accounting. Everyone working in economics must be able to understand the two essential elements of the balance sheet and the profit and loss account.

P. Samuelson

ARGUMENT

The book is addressed to those who want to open a business in Romania, to become entrepreneurs or managers and to accumulate necessary accounting information on starting and managing a business.

Accounting is the "ace up the sleeve" of any manager because, with the information provided, one can know the past, present and predict the future of a company.

This paper presents the theoretical elements of the concepts used in accounting necessary for any manager.

The book is intended for those interested in this field whose training can be completed with the ABC of accounting.

Authors

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INTRODUCTION

"There is for everything a time and a season for everything under heaven" and accounting is currently part of this temporal landmark. Business life is a reflection of a society that wants to earn but without risk, to profit without paying, to exist without assumption.

And for this there is Necher's famous formula *"the first rule of business is to keep accounts and neglecting them is the first step that leads to ruin"*.

The essential objective of accounting was and is to describe and measure reality, to remember, to separate and to act.

Accounting has been present in all known civilisations. Experts attest that it predates writing, and therefore facilitated development.

In the evolution of accounting in the service of humanity we can consider 3 historical stages:

- *Antiquity: accounting was essentially concrete and descriptive, it had a single purpose and therefore a single capacity to count, to reckon;*
- *the Middle Ages: accounting tied together isolated facts, which otherwise appear to be mere additions, and set themselves up as systems;*
- *Modern period: with concrete systems becoming accounting models.*

In antiquity, the first notable author was Hammurabi. Numerous cuneiform plates have survived from his time containing texts on the legal keeping of accounts. The Sumerians had numerous accounting sheets containing figures and texts that were displayed, mixed, descriptive elements, which were not intended to affect further operations but only to make checks.

The Sumerians had skilled financiers who used square tables effectively and could solve interest problems by arranging and adding them to capital.

In the time of the pharaohs, Egyptian accounts were less structured than Babylonian ones, but scribes were already making statistical and forecasting observations (e.g. keeping track of days and hours worked and estimating costs per day).

After 300 BC, Egypt adopted the Greek language and practices. The Zeno Papyrus contains letters, notes, accounts, bills, receipts, which have created a picture of the accounting of this period. The distinction between accounts of agricultural products and accounts of monetary flows is obvious; there was already a calendar, a diary containing details of daily records, general accounts summarising transactions over several days.

The Egyptians also knew how to falsify accounts in order to rectify certain situations, in particular supplies, outgoings, fictitious re-stocking, thus giving a more or less dubious account (for example, the barter between a day's work for a garment was accounted for in this way: one part was recorded in currency for the payment of a salary, then in exchange for the currency, the purchase of the garment was recorded, all this having no connection in fact with any manipulation of money).

In ancient Greece, accounting was quite developed. Here the temples acted as banks.

These real financial institutions knew and used cheques and policies during this period. The Athenians had a 10-member society of auditors who audited the public accounts and a college of auditors who audited the conflicting decisions taken by the first society.

The rigour of Roman law was in deep harmony with accounting precision. Keeping accounting records was, in Rome, for the head of the family an obligation similar to that of a modern-day merchant. Cicero made an important point about Roman accounting documents. The main document was the "book of expenses and earnings", together with the "adversaria" and "ephemeris", which allowed the preservation and recording of different types of transactions. But the most complete register was the "Codex rationum", which, like all registers, could be shown in court. Roman bookkeeping was the first to give a precise idea of rhythm in accounting work: daily transactions recorded in the "adversaria" and "ephemeris" were periodically reported, once a month, after possible reclassification.

In the Middle Ages, the international vocation of Roman civilisation gradually gave way to the autarchy of the feudal regime. This political development, coupled with economic difficulties, supported the scarcity of writing, technology and accounting signs. Since the 13th century, ancient knowledge has been reinvented. During the period of change, the use of Arabic numerals began, slowly but gradually replacing Roman numerals. The accounting preference for Roman numerals was marked by a conservative and typical spirit. It was difficult to change an operation written with Roman numerals rather than one written with Arabic numerals. With a little skill, the operation $33 + 33 = 66$ could be transformed into $88 + 88 = 176$. In Roman numerals, the same operation was written as $XXXIII + XXXIII = LXVI$, and to make it $LXXXVIII + LXXXVIII = CLXXVI$, inserting new numerals was much more delicate and difficult.

In the Middle Ages, bookkeeping took the form of a small register in which operations were recorded chronologically. In particular, transactions with customers, suppliers and bankers were described. Records have also been found in the form of articles, but the article recorded in the journalistic sense, i.e. closer to a description of operations than to analysis.

The diversity of production and service units, as well as the increasing complexity of transactions, led to the use of a simple-part accounting, characterised by the birth of accounts, describing a type of operation or summarising the activity of a production unit. In the form of these accounts, one column was reserved for increases and the other for decreases. Overlapping items and separate columns were replaced by "married" columns, i.e. side by side. Economic needs led to the creation of particular accounts, such as the "Capital", "Profit and Loss" account.

All known accounts of this period had many common features, such as: a diversity of accounts with a preponderance of accounts receivable and payable; a presentation effort that could not spare description. At the end of the Middle Ages, a great author made his mark on accounting life. Luca Pacioli, with his "Summa de

arithmetica, gemotrica, proportioni et proportionalita". The first author of an accounting work, the Italian Luca Paciolo describes and conceptually models an accounting already used in Italian cities. In his famous "Summa di Arithmetica, Geometria, Proportioni et Proportionalita", the mathematician includes in the chapter "Tractatus de computis et scripturis", a real milestone for the history of accounting. The treatise is the first encyclopaedia of management; he presented for the first time, in a coherent manner, the principles of double-entry (he did not invent it, but ensured its impetus in Christian Europe). He advocated the use of three accounting ledgers: the memoir, the journal and the ledger. He recommended taking inventory, of all the merchant's personal property and holdings, and last but not least, detailed the keeping of the various ledgers:

- **the memory** allowed, at the beginning, the recording of all operations without currency analysis;
- **the diary**, which contained debit and credit and was written in the form of articles with a dual purpose: to record operations chronologically and to express them in a single unit;
- **the ledger**, in which debits and credits were clearly and precisely differentiated account by account.

Pacioli paved the way for the successors but, did not indicate why and especially how we debate or believe. He has completed the codification of previous practices as a whole, establishing an algebraic link.

After Pacioli, an important accounting literature appeared in all European countries. But alongside some original stuff, many have more or less slavishly copied the reference stuff.

Much later, Claude Irson replaced the term "balance sheet" by "balance sheet". For him the balance sheet is a statement that juggles the records of the enterprise, period by period, not to exude wealth, but mainly to validate previous operations and prevent falsification of previous records and serve as a reliable basis for new records.

Mathieu de la Porte gave accounting the classical form it is known for today. He is credited with the current presentation of the balance sheet with assets on the left and liabilities on the right, as well as the principle of distinguishing the merchant's assets from the company's assets.

Bertrand Francois Barreme is the first author to advocate the use of the "balance sheet in the air", i.e. an accounting statement on a separate sheet rather than in a book with sewn sheets. After Barreme, Edmond Degranges published in 1795 his "Keeping of Light Accounts", which served as a point of reference for many generations of accountants. Up to the present day, accounting has made use of all the resources of modern mathematics, physics, computer science and communications technology. Accounting was and is a veritable language, and like many languages, it has great flexibility, a great capacity to resist the essential, a great ability to assimilate novelties and integrate them. An element of memory, an element of negotiation, a basis for action, accounting has an extremely important place even in modern management.

CHAPTER 1

NATURE AND PURPOSE OF ACCOUNTING

1.1 The importance of accounting

Accounting has emerged and evolved as production and marketing of goods has developed. The product of a long practical and theoretical activity, accounting has established itself as a system of knowledge and management of society's resources separated from its assets. Throughout history, accounting has evolved *in purpose from a technique for recording commercial transactions to a means of control and evidence*. For some specialists, accounting appears *as the technique or art of recording, classifying, processing and storing information expressed in terms of value relating to transactions and events of a financial nature taking place within the legal entity*. Although practice has anticipated the path taken by accounting, influencing applied accounting research, it is on the basis of these practical aspects that the functions, concepts, principles, procedures and scientific tools of this discipline have been shaped, giving it a scientific character. The modern definition of accounting starts from its basic function, *provision of financial data about the economic entity for use in decision-making*.

An economic entity is an enterprise or firm with its own assets, operating independently, with the purpose of producing products or marketing purchased goods. Accounting can thus be defined as *an information system that measures, processes and provides financial information about the enterprise, that is, how the capital invested by the owner is consumed and how this capital is increased*. Starting from the legal criterion, accounting captures aspects related to the exploitation of the resources owned by the enterprise.

Accounting captures the link between transactions and decision-making. Based on this, accounting measures the transactions carried out by the enterprise by collecting and providing information, shows how each transaction is carried out, the information provided is processed and stored, and is used in decision-making by users inside and outside the enterprise.

Accounting can be considered an "open cyber system", because recorded data about economic and social activity can be considered as inputs and data provided for decision making as outputs.

Accounting does not stop at the moment of data output, because the enterprise is set up to operate over a long period of time, and the activity carried out is resource-intensive and must produce results. Accounting provides information on the activity of the enterprise at equal periods, usually at the end of each year, on the financial and asset situation of the enterprise. In this sense, accounting can be seen as a service-providing activity, as the information produced is made available to individuals or legal entities who have to make decisions.

The accounting of the economic entity performs a number of functions, as can be seen from the following:

- *the recording and processing function* is the accounting function's ability to reflect operationally, accurately and comprehensively the economic phenomena occurring in an economic entity;
- *the information function* is the ability to provide information about the structure, economic phenomena and results of an economic entity at the end of a reporting period;
- *the management control function* is directly linked to the information function and is manifested by verifying the conservation and use of material and monetary values, as well as assessing the degree of fulfilment of the indicators forecast and compliance with financial discipline;
- *the forecasting function resides* in the accounting function's ability to provide useful information for economic and financial analyses;
- *the legal function* is manifested in the sense of carrying out operations of an economic and financial nature and the existence of assets and liabilities on the basis of legal supporting documents. At the same time, annual financial statements are the official documents of economic entities of public interest.

Accounting is defined as "*the whole of the operations of recording, on the basis of special rules and regulations, the movement of funds and materials in an institution; bookkeeping; or the science dealing with the theory of these operations*".

1.2 The object of accounting

Accounting is a science, an independent discipline, with its own object of research and scope.

The objectives of accounting are, on the one hand, to reflect and control the management of assets and liabilities owned by economic agents and, on the other hand, to monitor the activity carried out and determine the economic and financial results.

The object of accounting is the recording, calculation and control, in value terms, of the state and movement of assets, indicating their destination and source of origin, economic means, economic processes and financial results.

Luca Paciolo's name is linked to the first definition of the object of accounting: "everything that, in the merchant's opinion, belongs to him in the world, as well as all the great and small affairs in the order in which they took place".

Luca Paciolo is not the inventor of double-entry bookkeeping. It was he who promoted and popularized it. The ideas in Luca Paciolo's "Treatise on

Accounts and Entries" have influenced the accounting works of authors from different European countries for more than three centuries.

According to some authors, the existence of assets is the cause of accounting, because assets and their changes constitute the recordable matter of this discipline. Accounting studies the capital placed at the disposal of the enterprise by owners and creditors. This capital is studied by accounting from two aspects: the physical aspect of capital: economic assets intended to be exploited in the long or short term, and the aspect of the origin of capital - equity and liabilities.

Another defining aspect of the object of accounting is its scope. It has two dimensions:

- horizontally - delimits the spatial boundaries of the economic entity's accounting;
- vertically - delimits the links between the branches of the national economy.

Accounting is the main tool for knowledge, management and control of assets and results. The main objective of accounting is to provide a true and fair view of the state of the company's assets and results.

In order to achieve this objective, accounting must comply with the following principles:

➤ **The going concern principle**

If the economic activity of the enterprise is generally of a continuous nature, extending over several years, the financial life of the enterprise must be broken down into successive periods. This principle will apply when the annual accounts are drawn up and the business is resumed. Normally the undertaking is considered to be carrying on its activities continuously for the foreseeable future if it has no intention or obligation to liquidate or reduce the scope of its activities. Other accounting principles should also be recognised when recognising going concern.

➤ **The historical cost principle**

This principle is applied in almost all countries and has the advantage of simplicity and objectivity in the phenomena and transactions recorded in the accounts. Goods are recorded at purchase cost or production cost, depending on how they were obtained. In practical terms, this principle means that changes in the prices of goods recorded in the accounts are not taken into account. This gives a high degree of security as all incoming transactions can be checked against supporting documents. Applying this principle creates some difficulties when drawing up the annual accounts, as the result is altered by the fact that income and expenditure are recorded at prices from different periods, income at the current price and costs at the price level of the previous period (historical cost).

➤ **Principle of permanence of methods**

According to this principle, we must apply the same valuation methods to the assets and liabilities entered on the balance sheet and the content of the annual accounts. This principle allows the comparison of financial and accounting information relating to the activity of an undertaking over time and space. It is

considered that the accounting methods must be constant from one financial year to the next, if the straight-line method is applied for the calculation of depreciation or the FIFO (first-in, first-out) method is applied for the valuation of consumption of stocks, the same method must be applied in subsequent financial years. Therefore, if there is no exceptional change in a trader's situation, the annual accounts must be presented using the same accounting method.

➤ **Principle of exercise independence**

This principle involves dividing the activity of the enterprise into accounting periods and determining an overall result for each period in such a way as to express a ratio of effect to effort. Application of this principle involves taking stock of expenses and income, liabilities and receivables, in order to determine the result only on the basis of those expenses and income which relate to the current period.

➤ **Principle of prudence**

This principle requires a reasonable assessment of both the values of assets and liabilities and the facts and transactions carried out in the current year, so as to avoid transferring risks and losses of a probable nature that may affect the company's financial position and results in the coming period. The aim is to avoid overstatement of assets and income and understatement of liabilities and expenses. In the balance sheet, by setting up depreciation and provisions, the entry value of assets is reduced and balance sheet liabilities are increased. By writing off provisions in the profit and loss account, income is increased, so the amount of these amounts should be assessed as close to reality as possible.

➤ **No compensation principle**

The valuation of assets and liabilities must be carried out separately, assets must not be offset against liabilities, expenses against income, i.e. receivables against liabilities, financial income against financial expenses, income from the sale of goods against expenses for goods sold.

➤ **Material relevance principle**

In order to keep efficient accounts, we need to take into account only those transactions which are of particular importance for the financial and asset situation of the company. Certain purchases of goods can be entered directly on the expenditure side without using stock accounts if the value of the goods in question does not have a major impact on the financial result. This is the case with school supplies, printed matter, etc.

➤ **Income and expenditure recognition principle**

In order to establish the financial result, a correspondence between income and expenditure must be ensured. Every income is followed by an expense or vice versa, but this rule is not always followed. Depending on the timing of the recognition of income and expenditure, accrual accounting and cash accounting can be organised. In the case of cash accounting, expenses are recognised at the time of payment and revenue is recognised at the time of receipt. The financial result is the difference between receipts and payments.

In order to establish the financial results correctly on the basis of the resources consumed and the results obtained from the exploitation of capital, commitment accounting has been introduced. Expenditure is thus recognised when funds are committed, not when they are paid, and revenue is recognised when goods are sold, not when they are received, which creates many problems for the economic operator (VAT payable, income tax).

✦ **Principle of recognition of the financial result**

The financial result is based on sales revenue and the cost of that revenue, so the financial result is when the company has made use of what it has produced outside the company. To determine the financial result, accounting for the year must be organised, not accounting for the operation. Some transactions take place over a period of more than one year, so the financial result must be established at the end of the year, not at the end of a transaction.

1.3 Accounting systems

One of the main results of the evolution of the way in which businesses are organised is the modernisation of the accounting system to reflect the assets, financial situation and profit and loss, thus creating single and double-circuit accounting systems. The single-circuit system (monoist or integrated, Anglo-Saxon) organises the accounts in a single flow in the economic cycle, starting from capital, supply, manufacture, sale and production of products, both for operations concerning relations with third parties (external function) and for internal management (internal function). The dual-circuit system organises the accounts in such a way as to divide into separate circuits those which record items and transactions relating to exchanges and relations with third parties and financial results, and another circuit which records the production, costs and profitability of products and services rendered. This forms the financial accounting circuit and the internal management accounting circuit.

The purpose of financial or general accounting is to record all operations affecting the assets of economic agents, to measure the variations to which they are subject as a result of economic processes, and to calculate and exploit financial results. Its purpose is to present a true and fair view of the company's assets, financial situation and results by drawing up summary documents (balance sheet, profit and loss account and notes), following schemes which are compulsory both in form and content for all asset units.

Management or internal/managerial accounting is mainly aimed at controlling production factors in order to obtain products, works, services at minimum cost. It is organised by each asset unit according to its specific activity and needs. Its main objective is to calculate production costs, determine the results and profitability of products, draw up income and expenditure budgets by type of activity, sector, product, monitor and control the implementation of the budget in order to know the results and provide the necessary data for the company's management decisions.

By separating financial accounting from management accounting and achieving accounting dualism, the functions of accounting are as follows:

Financial accounting

- full recording of transactions;
- external financial communication (informing third parties);
- judicial and tax verification and evidence tool;
- management tool;
- providing the information needed for macroeconomic synthesis;
- information for financial analyses.

Management accounting

- determining the costs of sectors, products, inputs and services;
- determination of margins and analytical results by product;
- producing and providing information for the preparation of income and expenditure budgets and forward accounts;
- producing and providing updates of the indicators in the management (dashboard);
- producing information to measure performance: profitability, productivity at product and sector level.

From the point of view of how economic transactions are recorded in the accounts, accounting is double-entry and/or single-entry.

Double-entry accounting takes into account assets and liabilities valued in monetary terms during their movement and transformation in two respects:

- material composition aspect;
- the aspect of how it is procured, acquired and trained.

With double-entry bookkeeping, all economic operations concerning the movement and transformation of assets and liabilities are in a permanent balance; assets always equal liabilities. Single-entry accounting reflects the assets and liabilities according to the principle of simple recording, i.e. only their nature is recorded, without reflecting in the same entry the manner of their acquisition, formation or origin.

1.4 The accounting method

Accounting, like any science, has its own method of research. The features of the accounting method are that property is doubly represented, in the form of assets and their sources of formation, and that it constantly reflects the changes they undergo. Accounting therefore has a single research method, made up of a set of independent procedures, some of which are specific to the accounting method, while others are found in other sciences. The procedures specific to the accounting method are: the balance sheet, the accounting account and the trial balance.

The balance sheet is the process of presenting the situation of assets at a given time, both in the form of tangible items, called "assets", and in the form of the sources that formed them, called "liabilities" in value terms. This is the overall expression of the elements making up the assets.

The balance sheet is an important management and control tool.

The balance sheet is the process that shows the existence of, and all changes in, a single item of assets and liabilities. The account reflects the dynamics of the assets in detail for each individual. Specific to the accounts is the double recording of economic transactions, ensuring their accuracy and mathematical control. The expression is made using both the monetary and natural yardsticks.

The trial balance is the process used to periodically check the accuracy of the data recorded in the accounts and to centralise this information in order to give an overview of the assets and their movement over a period. By presenting the situation at the end of a period, the trial balance is also used to draw up the balance sheet, thus linking these procedures. Accounting procedures common to other economic disciplines are documentation, valuation, calculation, inventory.

Documentation is the process by which economic transactions are recorded in the accounts by recording them in written documents called records. They are drawn up at the time and place where the economic operations take place and provide proof that they have taken place. Valuation is the process of expressing in monetary (value) terms all the means, processes, etc. reflected in the accounts. This process makes it possible to generalise and aggregate all the economic processes in the unit.

1.5 Financial and accounting information

Adequate information results from a possible harmony between the different structural components that overlap and complement each other.

"Information is a set of data that causes a change in the probabilities that the beneficiary expects, following the occurrence of future events"

The existence of a market implies the existence of a product. **Accounting information** is the product exchanged in the accounting information market. This product exists only in terms of the rules and norms that define it. Accounting information is a specific "legal" product because its production, presentation and dissemination must be regulated.

An *accounting information market must ensure* that the interests of shareholders and third parties are protected by favouring:

- a. the development of published accounting information in terms of quantity and quality;
- b. publication and understandability of accounting information (transparency);
- c. increasing comparability over time and space.

The value of information can be defined as the difference between the net benefit of making a decision after obtaining the information and the net benefit of making the same decision unaffected by the information.

The progressive globalisation of financial markets makes the need for adequate and competitive information increasingly acute. Accounting theorists have long recognised that the accounting information system is an integral part of

an organisation's control system and that accounting information predicts critical decisions that also influence the decision to provide information for control.

Accounting information in an entity can be classified into two broad categories: financial accounting information and management accounting information. Financial accounting information is intended for external users such as investors, employees, creditors, government or the general public and is referred to as summary financial statements, or financial statements for short. Annually, company directors must prepare a set of financial statements in standardised form, consisting of: *balance sheet, profit and loss account, statement of changes in equity, cash flow statement and accounting policies and notes to the balance sheet and profit and loss account.*

Management accounting information is intended for internal users, specifically management. This information is non-standardised, often non-monetary, and includes information on the unit cost of products, cost behaviour in relation to the volume of activity or profitability per product.

Reports are submitted to management at short intervals - monthly, weekly or daily - and are broken down into subdivisions of the company, called responsibility or profit centres.

The financial accounting system exists and operates on the basis of financial accounting information. On the basis of this information it is possible to know the financial situation of any economic entity of public interest and to assess its performance. However, before the information becomes the basic material of the financial accounting system, it undergoes a series of processing operations; before it reflects the financial result of the public economic entity, the data on the existence, circulation and transformation of assets undergoes a series of processing operations. Financial-accounting information is the raw material of the financial-accounting system, providing a consistent basis for determining results and for informed forecasting of future activity.

Accounting provides certain types of quantitative information for decision making and management of a company. Accounting information, for most stakeholders, has become a crucial source of information about the company. In order to provide relevant information, the accountant must follow the rules and principles on which the processing of accounting data is based.

Accounting should not only be used as a source of information that allows us to calculate the amount of tax liability and collect the necessary returns. Accounting, together with other financial management tools, should be a comprehensive data source for internal and external users.

Internal users or primary users of accounting information include management, employees and owners. External users or secondary users of accounting information include creditors, tax authorities, investors, customers and regulators.

Modern social development requires improving the quality of economic and accounting information. Information should respond flexibly to business requirements. Such information is useful and provides added value.

Thanks to this useful information from financial reports, it is possible to better understand the economic reality of the business. The information in the accounts should be sorted chronologically and systematically. Documents should be processed on a regular basis. According to the Financial Accounting Standard Board (FASB), information should be relevant and reliable.

High-quality accounting information enables the measurement of a company's performance and financial position, to assess costs and revenues, income, expenses and profit. This information is needed for management and company decision-making. Performance information helps company managers make more informed decisions about controlling the production process.

For accounting information to be relevant, it must be timely. Information that is not available when needed or is available much later loses its value.

The quality of accounting information presented in financial statements is influenced by accounting errors. These are transferred to the financial statements. Some companies require only mechanical application of accounting rules, while others rely on the judgement of a company's management and accountants. These decisions are errors - both intentional and unintentional. However, in terms of the quality of information, the source of these errors is irrelevant to both, to reduce the quality of accounting information.

The quality of accounting data influences the company throughout its lifecycle. As it states poor quality information can occur at all levels. In addition, he adds that unqualified employees, errors in the application of accounting principles, manipulation of results, inflation, violations of law, etc. are potential sources of poor quality information.

Primary data sources are records that describe certain economic transactions. For this reason, it is necessary to pay attention to the requirements of the records. General errors are usually made especially in accounting areas such as financial accounts, e.g. cash and bank accounts, cheques, bank loans and trade payables and receivables.

The financial-accounting activity of a public interest economic entity is closely interdependent with all the other activities organised and carried out within the entity, since it reflects and evaluates them in value terms. The financial-accounting activity comprises actions that ensure the efficient, effective and economic collection and use of resources and the recording and recording of economic events occurring in the entity, all of which are carried out with the aim of achieving the objectives set.

As a baseline for the financial accounting system, financial accounting activity has three characteristics: solvency, profitability and control. Accounting, as the science of business knowledge and management, in its processes of measuring, valuing and controlling assets, liabilities and equity, produces an important element - financial accounting information. Depending on the main types of accounting that have been defined over time, the product they provide is similarly defined but has different addressees and purposes. Thus, managerial accounting produces financial and accounting information whose main addressee is the management of the

economic entity of interest. In order to achieve the objectives set, but also to facilitate rigorous control and rapid intervention when deviations occur, the financial and accounting information is detailed and creates the prerequisites for good future planning of its activities.

Unlike managerial accounting, financial accounting produces financial and accounting information for external use. Financial reports, as they are the product of financial accounting, are used by third parties, by hierarchically superior bodies, by statistical institutions, by state bodies responsible for monitoring and controlling economic activities carried out in economic entities of public interest.

The need to bring financial accounting principles into line with tax law led to the emergence of tax accounting. It also produces financial accounting information for tax experts who, on the basis of data from the financial statements submitted by the public interest economic entity, produce tax planning and estimate the entity's tax liability as a taxpayer.

Forensic accounting emerged and developed amid the need to investigate cases of litigation or disputes requiring experts to express and substantiate their opinions on civil and criminal litigation requiring assessments of financial effects. The product of this type of accounting is financial accounting information which is intended for experts who carry out assessments of fraud, losses, etc..

Public accounting produces financial accounting information that measures the performance and financial position of public sector economic entities. This information is intended primarily for the external use of the entity and ensures rigorous monitoring of its financial performance in the context of existing budgetary constraints.

The dominant relationship in the life of a business is the relationship between its owners and its managers. This relationship must be judged in the context of how the enterprise is governed.

While the relationship between the managers and owners of the enterprise is a primary relationship in the governance of the enterprise, it is no less true that, at international level, accounting today has to meet the needs of a diverse range of users, and its offerings are increasingly social in nature.

Internal users are represented by managers. They rely on accounting information reflecting operating, investing, financing and treasury management operations to inform and make their decisions. In doing so, they use both the information generated by current accounting and that presented in annual or quarterly financial statements as the final products of accounting. With the internationalisation of Romanian accounting, they have a major role to play in accounting choices: defining the most appropriate accounting policy options for the company to reflect economic reality. Mandated by the owners to manage the company's assets and activities, managers have at their disposal the data provided by financial accounting, as well as those related to management accounting (which are intended exclusively for them).

External users are represented by the company's financiers, business partners, social partners, public authorities and other external users.

The funders are the users who potentially or actually make available the resources necessary for the undertaking to carry out its activities. Depending on the type of financing, in the context of the different types of enterprises, we will find:

- stock market financiers, if the companies are listed on the stock market;
- bank financiers, if companies raise external resources through bank loans;
- the public authorities as investors in autonomous regions and enterprises of national interest;
- other categories of financiers (e.g. financing through the conclusion and implementation of lease-financing contracts, also called finance leases).

It should not be overlooked that a financially sound enterprise pursues a policy of striking a balance between recourse to external sources of finance (as set out above) and the generation of its own sources (self-financing, through the depreciation of various fixed assets and the allocation of a representative proportion of profits to reserves).

Accordingly, financiers are represented by investors, lenders (especially banks), the state and government agencies, lessors (under finance leases), etc. In accordance with international accounting regulations, external users of information, as defined in the context of financing processes and operations, are investors and lenders.

Managers and the need for informed decision-making

In the case of small businesses, the manager usually coincides with the owner. In other companies, however, the large number of shareholders means that they cannot be directly involved in the day-to-day running of the business and delegate management authority to a group of managers.

Managers' information needs are mainly covered by reports that are not published to other users. These reports are usually based on both management accounting information and financial accounting information. Their nature varies from one company to another, depending on the type of activity.

Managers have immediate and full access to accounting information. They do not have to wait for, nor are they limited to, the information published in the financial statements. Although they benefit from information asymmetry compared to other categories of users, managers nevertheless pay particular attention to how the published information is perceived by them. Such interest is due to the fact that published financial statements inform third parties about the managerial capacity of the management team. In other words, managers use the information in financial statements not to make management decisions, but to communicate.

Investors and the globalisation of financial markets

Generally, the investors (shareholders) want to measure the return and risk of their investments, and based on this they make the decision to maintain, increase or reduce their contributions. Thus, investors are interested in the company's ability to realise future earnings.

The notion of ability to realise future earnings refers to the extent to which the firm will adopt a strategy aimed at increasing its wealth, raising new funds and subsequently being able to convert the profits into cash. Investors usually reason in terms of cash flows, which have a tangible representation, and less in terms of net profit which, depending on accounting conventions, does not always reflect the real economic enrichment of the firm. Their reasoning also takes account of the fact that, as a rule, firms use part of their profits for self-financing.

Although shareholders appear to be the first victims of self-financing, in reality, self-financing increases net assets and the theoretical value of the share, which can lead to an increase in share price or a free share distribution. In these circumstances, the shareholder recovers through capital the part he has lost in the form of dividends.

Moreover, while distributed profits are subject to numerous cascading tax levies in most countries, reducing the amount actually available to shareholders, stock market capital gains are less taxed.

However, shareholders also want information on the dividend, as it is not just a cash transfer. It and its long-term growth rate convey a wealth of information about the company's prospects.

As for potential investors, they want to be able to calculate the rate of return they are entitled to expect from the company in order to invest their funds, taking into account the risk attached to their investment and the opportunities available in the market.

Creditors and the peculiarities of the banking market

Bank creditors are third parties who lend to companies in order to make a profit on these loans. For this reason, they are interested in the borrower's ability to make a profit, which is the only source of interest on the loans. But since only part of the profit remains at the company's disposal, banks pay particular attention to dividends, ensuring that their distribution does not reduce the economic capital of the *entity concerned*.

In addition, bank lenders want to ensure that the company will be able to repay the loans as they fall due.

In calculating the ability to repay loans, they do not take into account either historical cost or fair value. For reasons of prudence, they take the worst-case position and value assets and liabilities at their liquidation value. As a result, a number of assets (e.g. formation expenses) are ignored, others are systematically decreased while, to ensure a margin of security, liabilities are systematically increased. Banks also pay particular attention to the liquidity indicator. Liquidity

indicates the degree to which the firm's assets are liquid (cash or cash equivalents), allowing it to pay its debts and benefit from new investment opportunities.

Trade partners

The company's business partners are customers and suppliers.

Customers are interested in the company's ability to continue in business, and therefore to sell goods or provide services, for the foreseeable future.

Customers' information requirements are met to some extent by the profit and loss account and balance sheet.

Suppliers are interested in the extent to which the debtor company will be able to meet its financial obligations. This interest is partly satisfied by the balance sheet, which provides information on the resources available to the company, the debts it has incurred and the liquidity of its assets. Suppliers also want to know the likelihood of the company continuing in business and pay particular attention to its growth prospects, as any growth could have consequences for the volume and value of orders placed with them. These information requirements, however, relate to the future and cannot be adequately satisfied by information in the annual financial statements, which relate mainly to the past.

Employees: social pressure and staff benefits

The pressure exerted by employees and their unions on the provision of accounting information can be motivated in different ways:

- accounting information is relevant to the assessment of the company's future prospects, job security and the validity of pension plans;
- the accounting information allows an assessment of the fairness of the wages paid by the enterprise;
- information helps employees to increase their involvement in the company's work and their interest in work;
- information is a natural right of employees.

"Employees and trade unions are interested in the company's performance and prospects in terms of wage bargaining and job security. They also need information on sectoral performance in order to be able to check and understand managers' decisions to expand or restrict particular activities. Lack of information can lead to mistrust and problems in industrial relations." In other words, to assess the viability and prospects of a company, employees need to look at it as a whole. Then, using sectoral information, they will be able to better understand how their own activities fit into this whole. Because whether wages are determined in a more or less decentralised way, depending on the company, the viability of the sectors for which employees work will have an important impact on their job security.

The employees' interest also sometimes concerns information which goes beyond the current financial accounting, such as: the production programme, the general trend of orders, the employment situation in the undertaking, the measures planned for the improvement, renewal, transformation of work equipment or production and operating methods and their impact on working conditions. The

information requirements of employees and trade unions are only partly met by the profit and loss account and the balance sheet. Better satisfaction of these requirements requires additional information to be provided, either in the explanatory notes or in a social balance sheet.

Public administration between macro-accounting, fiscal and interventionist functions

The public administration is responsible for the country's economic policy. In order to achieve its economic objectives, it needs financial and accounting information. In other words, by involving itself in the process of accounting standardisation, the government is trying to ensure that it gets the information it needs.

In addition, national accountants and statisticians use accounting information for analysis at a very aggregate level (macroeconomic summaries) and at a detailed (micro) level. Their information needs, expressed in terms of economic variables to be measured, relate mainly to:

- measurement of the production of goods and services and its use (intermediate consumption, investment, exports, etc.);
- measurement of income from production and its distribution between the various production factors (shareholders, employees, creditors, government, etc.)
- measurement of accumulation (physical and financial investment) and the method of financing (self-financing or borrowing), description of assets, changes in their structure and financial relations between agents.

As a user, however, public administration is most often represented in the accounting information market by the tax administration, as accounting information is used to establish the basis for the calculation of taxes and duties. Thus, for the calculation of the current corporation tax, the accounting result is taken as the starting point, corrected by non-deductible expenses and tax deductions. In addition, accounting provides the information needed to calculate value added tax, tax on dividends, tax on buildings, tax on wages, etc.

In exercising its interventionist function, the public administration uses accounting information to analyse various applications for subsidies or low-interest loans for various economic activities.

Financial analysts and business diagnostics

Financial analysts take raw information and transform it into another type of information, reflecting their ability to understand, synthesise and interpret information as raw material. Specifically, they perform three types of information-related activities:

- a) the search for private information that is not publicly available;
- b) analysing, processing and interpreting information for forecasting purposes (predictive analysis);

- c) analysis of past performance (retrospective analysis). Their relationship with accounting information is not a simple one: on the one hand, accounting information is a factor of production for analysts and, on the other hand, the same information is a competitive product on the market for *analytical reports*.

The information offer is the set of information available to different user groups. It ranges from verbal responses to shareholder questions at annual meetings to written communications such as physical production reports and summary documents. In addition, information flows from different sources vary in intensity over time.

CHAPTER 2

REPORTING INFORMATION ON THE FINANCIAL POSITION

2.1 Balance sheet and financial position of the economic entity

Accounting uses its own process called the balance sheet to represent assets.

"The balance sheet is a summary document which, at a given time, shows all the resources available to the undertaking and all the allocations made".

The balance sheet drawn up at the end of the accounting period describes separately the assets and liabilities of the enterprise. Assets consist of assets held by the undertaking and receivables, structured according to their degree of liquidity, and liabilities consist of equity and debts incurred by the undertaking and not yet repaid, structured according to their degree of collectability.

Other definitions of balance sheet in the literature:

The balance sheet is "a summary computation showing the financial position of the enterprise at a given point in time".

As a reflection of the balance sheet "the balance sheet drawn up at the end of the accounting period describes separately the assets and liabilities of the enterprise".

At some point, "the balance sheet indicates the state of resources and means of an enterprise, expressing financial equilibrium".

The mathematician Luca Paciolo pointed out the need to draw up a balance sheet when double-entry bookkeeping became a system. The documentary and informative economic nature of the balance sheet was revealed by Jaques Savary in 1673 as "an instrument for controlling accounting records and for knowing the economic and financial situation of the enterprise".

Simply put, the balance sheet is the summary document that shows the state of affairs of an enterprise at a given point in time.

For more than half a millennium, accounting has operated under the double-entry principle. However, it was not until the 19th century, thanks to large industrial and commercial enterprises, that the balance sheet began to be used to regularly analyse and measure assets and liabilities, and the profit and loss account to measure results.

In a general formula, which can only be a simplifying one, the balance sheet has been and is considered a summary document which makes it possible to know, at a given time, the assets of a trader, whether a natural or legal person. Such a formula establishes the *assets and liabilities as all the rights and obligations of the trader*.

Also, the balance sheet was, and still is, recognised as a static tool. The static approach to the balance sheet was opposed, with the work of Eugen Schmalenbach, by a diametrically opposed, dynamic approach. He found that it is

more important for managers to measure the health of the company than to know the intrinsic value of the elements that make up the two parts of the balance sheet, assets and liabilities.

The balance sheet can be approached conceptually, financially and technically.

Conceptually, the balance sheet can be defined as a representation of the uses and resources available to an asset entity at a given point in time.

This representation takes the form of a balance reflecting the value balance between uses, known as heritage assets, and resources, known as heritage liabilities.

From a financial point of view, the balance sheet is analysed as a description of the resources invested (liabilities) and the allocation of these resources (assets), thus allowing a start to be made on interpreting the financial situation of an enterprise.

From a technical point of view, the balance sheet is completed on the basis of the debit or credit balances of the accounts indicated by the balance sheet layout, balances taken from the trial balance of the accounts, drawn up at the end of the period for which the balance sheet is completed.

Tangible and intangible assets, as well as the rights and obligations making up an asset, are referred to as 'assets' and 'liabilities' in the balance sheet.

2.2 Patrimonial assets

Balance sheet assets are represented by "economic means" differentiated among themselves according to: their own characteristics, value, duration of use and mode of use.

Assets comprise all the economic goods at the disposal of the economic entity, classified into fixed assets and current assets. Assets also include prepaid expenses.

❖ Non-current assets comprise those economic assets of an investment nature, of lasting use, with a period of use and liquidity of more than one year. They are classified as intangible, tangible and financial fixed assets.

Fixed assets are economic assets that have become part of the company's assets as a result of long-term investment. So capital provided by owners and creditors is intended to be used for a period of more than 1 year. Fixed assets (fixed or stable) are characterised by the following aspects:

- *remain in the heritage for more than 1 year without changing their original state;*
- *the capital invested in the assets is recovered during their period of use or when they are removed from the assets;*
- *low liquidity.*
- *These assets are also called fixed assets and are represented by:*
- *intangible assets;*
- *tangible fixed assets;*

➤ *financial fixed assets.*

Intangible assets (intangible assets or non-tangible assets) comprise those values that do not have a tangible form, namely:

- Formation expenses (expenses of formation or merger, such as fees, registration expenses, incorporation, share issue, market canvassing, advertising));
- Research and development expenditure includes economic resources allocated to investment, new technologies, new product development or to broaden the product range;
- Concessions, patents, licences, trademarks refer to expenditure incurred for the acquisition of the rights to exploit a good, service, in the case of concessions, a patent, know-how, a licence, a trademark and other similar industrial and intellectual property rights;
- Other intangible assets include assets such as computer software created by the enterprise or acquired from third parties for use for its own purposes;
- The goodwill comprises expenditure incurred to maintain or develop the business potential of the enterprise: clientele, sales force, firm, market segment, logo. Goodwill is recognised in the accounts as an intangible asset when it results from the acquisition of another enterprise whose acquisition cost is higher than the market value of the net assets acquired (assets purchased less liabilities assumed);
- Advances and intangible assets in progress are fixed assets that have not been completed at the end of the financial year, including amounts paid on account of intangible assets

Tangible fixed assets (fixed or tangible assets) comprise all tangible assets that are used for a long period of time in a firm's activity, such as land and fixed assets (buildings, special constructions, machinery, equipment, working installations, measuring, checking and regulating apparatus and installations, means of transport, livestock, plantations, tools, furniture, office equipment, etc.).

A fixed asset has a value greater than the limit set by law and a normal period of use greater than one year. If the tangible goods purchased or produced by the enterprise are not completed, they are called investments in progress.

Tangible fixed assets lose value over time as a result of wear and tear caused by their use (physical wear and tear) and technical progress (moral wear and tear). The accounting recognition of the loss of value suffered by tangible fixed assets (excluding land) and their inclusion in costs is called depreciation. Land is considered to have an unlimited useful life and is the only item of property, plant and equipment not subject to depreciation.

Financial fixed assets (financial or portfolio investments) comprise financial assets invested by the enterprise in the assets of other companies, such as equity securities, receivables attached to equity holdings, loans, etc.

Equity securities are securities in the form of shares, stocks and similar securities invested in the assets of other enterprises. Owning these securities enables control to be exercised over the management of the unit which has issued

them, and dividends can be obtained if the unit makes a profit.

- Other non-current assets include securities other than the above categories which the enterprise holds and has no intention or ability to resell.
- Receivables from participating interests represent the rights conferred by the operation of granting long-term or medium-term loans to companies in which the enterprise has a participating relationship. Other non-current assets are guarantees and deposits lodged by the enterprise with third parties to ensure the proper performance of obligations.

❖ Current assets comprise economic assets that change material form and usefulness in the economic cycle and have a turnover period of less than one year.

The dynamic nature of these heritage assets is also highlighted by the different forms they take in some phases of activity, for example: cash assets are transformed into materials, raw materials during the supply phase, which in turn, in the production phase, become products, products, and which through valorisation, in the disposal phase, temporarily become receivables (customers) or cash assets again.

Current assets are economic assets that are in the form of cash or are converted into cash within a period of less than 1 year. In practice and in theory these assets are considered current because they change their condition within an operating cycle. They are also called circulating capital. They are characterised by the fact that:

- are intended for exploitation for a period of less than 1 year;
- change shape after use;
- are much more liquid than fixed assets.

Current assets are grouped according to liquidity into physical assets, receivables and cash. Current assets are classified into inventories and work in progress, receivables, investments and cash in hand.

Stocks and work in progress

Stocks are all goods held for sale in the same condition or after processing in the production process, or to be consumed when first used. They take the form of raw materials and consumables, work in progress, semi-finished products, finished products, packaging, etc.

- Raw materials are intended to be used in the production process, they participate directly in the generation of products and are found in the finished product in whole or in part, either in their original state or processed.
- Consumable materials (auxiliary materials, fuels, packaging, spare parts, seeds, planting material, feedingstuffs) are intended for use in the production process and participate in or assist the manufacturing or operating process without, as a rule, being present in the finished product.
- Stocks held with third parties are various goods which are in owned by the enterprise, but which are physically in the custody of, processed by or

consigned to third parties.

- Inventory items, i.e. goods with a value less than the limit laid down by law to be considered fixed assets, regardless of their period of service or with a period of less than one year, regardless of their value, as well as goods assimilated to them (protective equipment, work equipment, special clothing, instruments, testers, etc.).
- Work in progress is production which has not gone through all the processing stages laid down in the technological process, products which have not yet undergone technical testing and acceptance or which have not been fully completed.
- Semi-finished products are products for which the technological process has been completed in one manufacturing stage and which are to be passed on to other manufacturing stages or delivered to third parties as such.
- Finished products are products that have gone through all the stages of manufacture foreseen in the technological process and are stored for sale to third parties.
- Residual products are products resulting from the manufacturing process, such as rejects, recoverable materials, waste.
- Animals include animals and birds reared and used for breeding, animals and birds for fattening to be used, bee colonies and animals for the production of wool, eggs, meat, milk and fur.
- Goods are those goods which have been purchased by the enterprise with a view to resale.
- Receivables or amounts in course of settlement refer to amounts of money, works or services, goods advanced temporarily to other natural or legal persons and for which an equivalent in the form of money or a service is expected to be received. These may be stocks sold to customers, cash advances given to employees travelling on business. People who owe money to the business are called debtors.

The most significant trade receivables are made up of amounts due from customers and notes receivable.

- The debtors of trade receivables relating to the sale on credit of goods, works or services belonging to the operating cycle of the enterprise are called customers.
- Receivables are negotiable instruments in the form of bills of exchange, promissory notes, etc., which attest to the existence of a receivable in commercial relations which will be collected in the short term, usually up to 90 days.
- Intra-group claims arise in settlement relationships between the parent company and its subsidiaries.
- Claims on subscribed and uncalled capital are claims that the enterprise has on its shareholders in respect of subscriptions to share capital made and not paid up.
- Other claims arise in the enterprise's relations with staff, the state budget,

social insurance, social protection, sundry debtors, etc.

Marketable securities and money market paper comprise all economic securities that take the form of money or fulfil this function.

They relate to investment securities, cash and other financial or treasury assets.

- Investment securities refer to short-term stocks and bonds, and unlike equity securities, which are held for more than one year, the turnover period of investment securities is generally less than one year.
- Cash in lei and foreign currency refers to cash in hand, deposits held in bank accounts or other assets that can be immediately converted into currency.

Also included in the category of liquid funds are cheque books with or without limit of amount, letters of credit and cash advances. Cheque books with a limit on the amount include cash in value documents used to make payments; they are held in a separate account at the bank. A credit note is a form of settlement which gives suppliers the security of collection.

The liquid assets shall be kept in a separate account at the supplier's disposal, from which payments shall be made to the supplier as and when goods are delivered, works are carried out or services are rendered.

Cash advances represent the cash available for distribution to employees for the purchase of goods or services and which are subsequently settled. Other financial or treasury assets are classified as include postage or revenue stamps, vouchers or tickets for travel, treatment and rest.

❖ *Accruals and deferred income* are values that do not yet have a defined status and will take their final form during the next reporting period. For example: prepaid expenses, assets in course of settlement, rents, taxes, interest paid in advance, unfavourable differences on the translation of debts and receivables into foreign currency (foreign exchange), etc..

2.3 Patrimonial liabilities

From a legal point of view, liabilities comprise equity and debts, from an economic point of view, the classification is made into equity and debts (financial and operating), and from a financial point of view the amounts are grouped according to their due date (term of payment) into permanent, long-term capital and short-term debts.

There are three groups of liabilities:

- A. OWN AND SIMILAR LIABILITIES
- B. LIABILITIES ATTRACTED AND BORROWED
- C. REGULATORY LIABILITIES

A. OWN LIABILITIES represent the asset holder's own financing of the asset through his material contribution in the form of individual capital (for sole proprietorships), share capital (for partnerships) and self-financing.

This category also includes the various reserves made up of profits, investment grants from the budget and various funds such as: development fund, profit-sharing fund, other funds..

B. BORROWED AND ATTRACTED LIABILITIES, also known as debts, show the financing of assets by raising capital from third parties or by borrowing from banking institutions.

Debts refer to bank loans, loans from bond issues, trade debts to suppliers, tax debts, wage debts, social debts, debts to shareholders from capital operations, dividends, etc.

Bank loans refer to both long-term and medium-term financing and short-term treasury loans granted by banks. They bear interest and are secured against the assets of the enterprise.

Trade payables to suppliers arise in relation to the various assets from which the enterprise obtains raw materials, materials, works and services.

Tax, wage and social security liabilities include obligations to pay taxes, wages and similar entitlements due to employees, social security contributions, unemployment insurance and health insurance contributions.

Liabilities to shareholders from capital operations, dividends, etc. Represents obligations to shareholders for capital to be repaid, dividends to be paid, and intra-group liabilities.

Other types of liabilities, such as liabilities to customers who have paid in advance for goods or services to be delivered or rendered by the firm (so-called customer-creditors).

Provisions for risks and charges are liabilities of the company with uncertain timing or amount, and are generally established at the year-end. The main difference between provisions for risks and charges and other types of corporate liabilities is the uncertainty affecting the former in terms of size or maturity.

C. REGULATORY LIABILITIES are sources that do not have a definitive status.

Deferred income is that amount which provides the allocation for each financial year only its own revenue. They relate to investment grants and revenue entered in advance.

Investment grants or capital subsidies are obtained from the budget or other non-repayable sources and are intended for the acquisition or creation of fixed assets (grants for the purchase of equipment) or the financing of long-term activities (e.g. development grants for enterprises creating new jobs).

2.4 Double representation of assets in the balance sheet

The dual representation of assets and liabilities achieves the causal link between the object and method of accounting and is a basic principle of accounting.

By "double representation" is meant the reflection in the accounts, by means of data, of the assets of an establishment in their two aspects: tangible and intangible and abstract in terms of their origin.

The dual presentation of assets and liabilities is required by the need to know the economic and financial situation of each asset and liability unit and is done in the accounts using a specific procedure called the 'balance sheet'.

The dual representation of assets and liabilities in the balance sheet is made in the two separate sections of the balance sheet called **assets** and **liabilities**, which will be entered respectively as "*balance sheet assets*" and "*balance sheet liabilities*".

Capital can also be approached from another point of view: **uses = resources**. these are materialised as follows:

Uses = means representing the existence of assets and

Resources = sources represented by stocks of liabilities

2.5 Content and structure of the balance sheet

The term balance comes from the Italian word "bilancia" with Latin origins: bi and lany (two thimbles). Meaning a balance with two arms in which the ASSETS are clearly marked on one side and the LIABILITIES on the other.

The balance sheet is an accounting procedure for the *representation of assets and is presented* in the form of a table with two distinct sections: ASSETS and LIABILITIES.

Within the ASSETS are delimited:

- permanent uses of resources in the form of investments;
- temporary uses in the form of stocks, receivables, cash;
- losses arising from unprofitable activity on the use of resources.

Within LIABILITIES are delimited:

- permanent resources provided by the owner (associates or individual);
- temporary resources provided by third parties (suppliers, banks, bondholders);
- resources in the form of realised profit.

The components of the assets and liabilities are entered in the balance sheet only in terms of value and grouped together as balance sheet items or balance sheet items.

*) If the balance sheet item comprises balance sheet assets, it is entered to the left of the balance sheet (i.e. under Assets) and will be an "**asset item**", for example: Buildings, Consumables, Livestock and poultry, etc.

*) If the balance sheet item comprises balance sheet liabilities it is entered on the right of the balance sheet (i.e. in Liabilities) and will be a "**liability item**", e.g. Share capital, Short-term bank loans, Suppliers, etc..

The order in which assets and liabilities are recorded in the balance sheet is based on the importance and weight of each item.

Between the two sections of the balance sheet there must be a balance sheet (value) equality, an equilibrium relationship, due to the fact that:

- the two sections (Assets and Liabilities) show the same assets and liabilities, but from the two different points of view;
- each asset has an origin, and a source of financing once created generates an asset.

This balance sheet equality is expressed graphically:

$$\boxed{A = L}$$

By its content, the balance sheet has an economic and a legal significance.

Thus, from an economic point of view, the balance sheet shows the situation of the assets and liabilities, and from a legal point of view, the balance sheet shows the situation of the rights of the unit and its obligations.

The balance sheet is a mandatory accounting document and is drawn up at certain intervals: periodically (quarterly, half-yearly) and annually (at the end of the year). The data in the balance sheet serve, on the one hand, to summarise and generalise the assets and liabilities existing at the end of the period and to characterise the activity carried out in the establishment during that period, and, on the other hand, as a basis for the process of re-establishing them in the following period. Hence the term '**closing balance sheet**', which also reflects the economic and financial results for the period in question, and the '**opening balance sheet**' (initial balance sheet), on the basis of which the accounting cycle is restarted.

The balance sheet, as an accounting process, is a management tool that presents the actual situation of the assets at a given point in time, but also the economic and financial results obtained over a period of time. These results may be in the form of Profit or Loss.

From an accounting point of view, **losses** represent the amount of goods consumed, which could not be covered by own income - so they are assets, while profit represents the amount of income in excess of expenditure, an important source of financing - so it is a liability.

2.6 Changes in assets and liabilities and their reflection in the balance sheet

The production activity that takes place in economic units, materialised in various economic operations, leads to a change in assets. Each economic operation produces a change in the structure and content of the balance sheet. After each economic operation it is necessary to draw up a new balance sheet reflecting the change and the new situation of the assets and liabilities.

Changes in the balance sheet take account of the following general rules, irrespective of the content of the economic operation, the time when it is carried out and the place where it takes place:

- 1) Each economic operation simultaneously changes two balance sheet items;
- 2) The economic operation changes the two balance sheet items by the same amount;
- 3) The changes in the two items are always opposite: either in sign (plus + or minus -) or in balance sheet position (asset or liability);
- 4) Regardless of whether the total amount of the balance sheet changes or not after the recording of the economic operation, the equality between assets and liabilities remains permanent (as a basic law of accounting).

Using the symbols of A - for asset, L - for liability and X - for modification, these general rules can be written as balance sheet modification formulas as follows

- 1) Increase one asset item by a certain amount and at the same time and by the same amount decrease another asset item, the liability remaining unchanged:

$$A + X - X = L$$

This formula is used to reflect a structural change in the composition of balance sheet assets.

ASSETS	BALANCE SHEET	LIABILITIES
+X	No change	
-X		
A + X - X = L		

- 2) Increase one liability item by a certain amount and at the same time and by the same amount decrease another liability item, the asset remaining unchanged:

$$A = L + X - X$$

This formula is used to reflect a structural change in the composition of balance sheet liabilities.

ASSETS	BALANCE SHEET	LIABILITIES
No change	+X	
	-X	
$A = L + X - X$		

These two changes are called **permutative movements** and are characterised by the fact that they do **not change** the total value of the balance sheet.

- 3) Increase an asset item by a certain amount and at the same time increase a liability item by the same amount:

$$A + X = L + X$$

This formula is used to reflect a change in structure (in the + sense) in the composition of both balance sheet assets and liabilities.

ASSETS	BALANCE SHEET	LIABILITIES
+ X	+ X	
$A + X = L + X$		

- 4) Decrease an asset item by a certain amount and at the same time decrease a liability item by the same amount:

$$A - X = L - X$$

This formula is used to reflect a change of structure (in the sense of -) in the composition of the whole estate.

ASSETS	BALANCE SHEET	LIABILITIE
- X	- X	
$A - X = L - X$		

These changes are called **opposite movements** and are characterised by the fact that they **change** the total value of the balance sheet in the sense and amount of the economic transaction recorded.

Reflecting changes in a company's assets and liabilities by drawing up a new balance sheet after each economic operation is not done in practice. This is because, on the one hand, it is not economically justified and, on the other hand, because several economic operations can take place at the same time.

This situation is resolved by using 'accounting accounts'.

2.7 Profit and loss account and financial performance of the economic entity

The profit and loss account is the financial statement that measures the success or performance of an economic entity's business for a given period. It is the financial performance of that entity. Given that the accounting results are the consequence of applying a series of accounting assumptions and principles, and above all of the independence of the financial years, the recognition of income and the linking of expenses to income, the importance we attach to this summary document must be accompanied by a dose of caution.

The profit and loss account provides investors and creditors with information necessary to forecast the values, timing and cash flow generating capacity of the economic entity. In this way, investors can more accurately assess the economic value of the enterprise and creditors can determine the extent to which the economic entity will be able to repay its debts.

This financial statement provides information to enable an assessment of the past performance of the economic entity. And even if a positive past performance is not a guarantee of future success, it at least provides an update on the most important trends. Because when there is a rational correlation between past and future performance, the estimation of future earnings and cash flows should not be questioned.

On the other hand, the income statement provides users with the information needed to determine the risk or degree of uncertainty in relation to future cash flows.

Because by providing information that explains the elements that lead to benefits - income, expenses, gains and losses - this financial statement actually highlights the relationships between the components mentioned. It can also be used by other categories of users. Customers want to be informed about the extent to which the economic entity can provide them with the goods and services they need. Trade unions want to examine the results with a view to negotiating new collective agreements. In turn, public authorities use information on results to inform their economic and fiscal policies.

CHAPTER 3

DOUBLE-ENTRY ACCOUNTING SYSTEM

3.1 The accounting account - importance, functions, content and graphic form

The balance sheet - as an accounting procedure - presents the overall situation of the assets and liabilities existing in the establishment at the date of its preparation. However, it is not possible to follow the movement of assets and liabilities continuously by drawing up successive balance sheets, both because of the large volume of calculations and the need for detailed knowledge of each individual item. This need for detailed knowledge of the actual situation and of all the changes in the assets and liabilities is met by means **of accounts**.

An account is an economic calculation, presented in a special form, with the help of which the existence and movement of a given asset (economic means, economic process or source of formation) is traced in value (sometimes also in quantity).

The name "account" comes from the Italian word "conto", which means "account" or "bookkeeping" and which also gives the name "accounting".

There are similarities between the two accounting procedures, the balance sheet and the account (both deal with assets and liabilities), but also differences (the balance sheet shows the totality of assets and liabilities, while the account shows the existence and all changes in each asset and liability).

The account is the most important accounting process because of the functions it performs:

- **economic function** (reflects the existence and movement of economic means, processes and sources);
- **the statistical function** (records all values relating to the existence and movements of assets);
- **the calculation function** (determines by calculation the existence at any time of the items of wealth);
- the control function (checks how economic resources and sources are used);
- **the grouping function** (records economic transactions by type of movement - increases or decreases).

Changes that occur due to economic transactions can be in the '+' direction (increases, increases, additions, gains, etc.) and in the '-' direction (decreases, decreases, withdrawals, reductions, etc.) (9). The account must be in a form which allows the recording of '+' and '-' transactions separately, i.e. two sections, These two sections are called:

left - Debit - simbol D

right – Credit – simbol C

In addition to these two sections, the account also has other mandatory elements that make **up the account structure**. Each account must contain the following elements in its structure:

- 1) **The title of the account**, indicating the asset item for which it is kept. For example, 'Buildings' account, 'Land' account, 'Suppliers' account, etc;
- 2) **The two sections (DEBIT and CREDIT)** in which "+" and "-" economic transactions are recorded; debiting an account means recording an amount to the debit of the account, and crediting an account means recording an amount to its credit.
- 3) **Account balance** represents the total of all amounts of the same kind booked in a period of time. It may be **debit or credit** depending on the part of the account in which it was established;
- 4) **Explanation** of the economic transactions recorded in the account such as: date, type and number of the registration document, etc;
- 5) **The balance of the account** shows the existence at a given time of the asset item. It is obtained by the difference between the totals of the two sections of the account. The account balance can be:

debtor	if	$D > C$
lender	if	$C > D$
none, zero	if	$D = C$

Each account can have at any one time only one kind of balance, debit, credit or zero.

Depending on the period when it is calculated, the balance can be: **initial and final**. The opening balance is the amount entered in the account at the beginning of the period and the closing balance at the end of the period. Opening balances are taken from the balance sheet and closing balances are calculated using the following formulas.

$$\begin{aligned} \text{F.d.b.} &= \text{I.d.b.} + \text{D.r.} - \text{C.r.} \\ \text{F.c.b.} &= \text{I.c.b.} + \text{C.r.} - \text{D.r.} \end{aligned}$$

in which the symbols have the following meaning:

- final debit balance (F.d.b.)
- final credit balance (F.c.b.);
- initial debit balance (I.d.b.);
- initial credit balance (I.c.d=b.);
- debit roll (D.r.);
- creditor roll (C.r.).

3.2 The rules of operation of the accounts

Balance sheet items are grouped into two categories - assets and liabilities, depending on the position in one or other section of the balance sheet. Linked to this, the accounts are also classified into two broad categories: asset accounts and liability accounts.

Asset accounts - reflect the existence of and changes in an asset item, i.e. balance sheet assets. For example, the " Property " account, the " Consumables " account, the " Cash " account, etc.

Liability accounts - reflect the existence of and changes in a liability item, i.e. balance sheet liabilities. For example, the " Equity " account, the " Suppliers " account, etc..

The recording of opening balances, changes of "+" or "-" and closing balances in accounts is done differently for the two categories of accounts:

1) Opening balances shown by balance sheet items are debited to asset accounts and credited to liability accounts.

At the beginning of each accounting period after the initial balance sheet has been drawn up, the 'opening of balance sheet accounts' operation, which consists of the transfer from the balance sheet to the accounts, also takes place.

This is done as follows: for each item on the assets and liabilities side of the balance sheet, an account is opened, which will bear the name of the item in question, and the amounts with which the items appear on the balance sheet are entered in the accounts, in the same part as the initial balances - those on the assets side (left) in debit (left) and those on the liabilities side (right) in credit (right).

		INITIAL BALANCE SHEET		
ASSETS			LIABILITIE	
asset items (initial debit balances)			liability items (initial credit balances)	
		A=L		
ACTIVITY ACCOUNT			LIABILITY ACCOUNT	
DEBIT	CREDIT		DEBIT	CREDIT
START			START	
SALD			SALD	

2) Movements (changes) of "+" and "-" are recorded as follows:

- *changes of "+"* are entered in the same part as the initial balances, i.e. in the debit of the asset accounts and in the credit of the liability accounts, they actually represent increases in value of the initial balances;
- *changes of "-"* are entered on the opposite "+" side (precisely to differentiate), i.e. to the credit of asset accounts and the debit of liability accounts.

ACTIVITY ACCOUNT		LIABILITY ACCOUNT	
DEBIT	CREDIT	DEBIT	CREDIT
„+”	„-”	„-”	„+”

3) Closing balances may be debit or zero for asset accounts and credit or zero for liability accounts and are calculated according to the formulas presented above.

At the end of the accounting period for balancing the value of the two sections of the account, the balances are entered on the reverse side (debit ending balance in credit and credit ending balance in debit).

After the accounts have been closed, the final debit balances are entered on the assets side of the final balance sheet and the final credit balances on the liabilities side of the final balance sheet - the final balance sheet with which an accounting period ends.

ACTIVITY ACCOUNT		LIABILITY ACCOUNT	
DEBIT	CREDIT	DEBIT	CREDIT
final debit balance		final credit balance	

ASSETS	FINAL BALANCE SHEET	LIABILITIES
Closing debit balances (asset items)		Closing credit balances (liability items)
A=L		

So each category of accounts (assets and liabilities) works differently according to the following rules of account operation:

- I. **Asset accounts** start to operate at the beginning of the accounting period by debiting the opening balance of the asset item in the balance sheet. During the accounting period they are debited with all the '+' of the asset item and credited with all the '-' of that item. At the end of the accounting period it may have a debit or zero ending balance.
- II. **Liability accounts** start to operate at the beginning of the accounting period by crediting the opening balance of the liability item in the balance sheet. During the accounting period they are credited with all the '+' of the liability item and debited with all the '-' of that item. At the end of the accounting period it may have a credit or zero ending balance.

Schematically, these rules are as follows:

Asset accounts		Liability accounts	
DEBIT	CREDIT	DEBIT	CREDIT
Initial balance „+”	„-” (Final debit balance)	„-” (Final credit balance)	Initial balance „+”

Knowing these rules, it is possible to define (in addition to the Assets and Liabilities of the balance sheet) the two sections of the account:

DEBIT - the section to the left of the account in which are recorded: the opening balance (item in the assets of the balance sheet), increases ("+") of an asset item and decreases ("-") of a liability item.

CREDIT - the section to the right of the account in which are recorded: the opening balance (liability side of the balance sheet), increases ("+") of a liability side and decreases ("-") of an asset side.

These two processes - balance sheet and account - are closely dependent on each other, the accounts originate from the balance sheet and the balance sheet is based on the data in the accounts.

3.3 Matching of accounts, accounting analysis, accounting formula and double entry in the accounts

The activity being carried out must be recorded in the accounts, using the balance sheet and the accounts.

Economic transactions always change two balance sheet items. If we want to show this using the accounts we will find:

First formula: $A + X - X = L$, where the two items are assets, one with a "+" and the other a "-". Instead of the two balance sheet items we will use two accounts, one asset account with "+" and the other asset account with "-".

According to the rules of account operation - the asset account with "+" is debited and the asset account with "-" is credited.

$$\begin{array}{rclcl} A & + & X & = & D \\ A & - & X & = & C \end{array}$$

Making the same reasoning for the following three balance sheet modification formulas, the following is found:

$A = L + X - X$	$L + X = C$
	$L - X = D$
	$A + X = D$
$A + X = L + X$	$L + X = C$

$$A - X = L - X$$

$$A - X = C$$

$$L - X = D$$

Thus, an account can only work together with another account, one modifying its left section - Debit, and the other the right section - Credit.

The link that is established between two accounts that change as a result of an economic operation is called the **correspondence of accounts**, and the accounts are **correspondent accounts**.

The correspondence of the accounts is mentioned in the form of an equality called the **accounting formula** and consists of three elements:

- 1) **the debiting account** (i.e. the account that changes its debit by an amount) and is written to the left of the equals sign;
- 2) **the account which is credited** (i.e. the account which changes its credit by the same amount) and which is written to the right of the equals sign;
- 3) **the equal sign "="** which is written between the two corresponding accounts.

Establishing the correspondence of the accounts and the accounting formula for each economic operation can be done with the help of the **accounting analysis** - a reasoning that involves the following steps:

1. knowledge of the nature of the economic operation (consumption, payment, production, delivery, etc.);
2. establishing the affected accounts by simultaneously changing them by the same amount (i.e. establishing the corresponding accounts for the given economic transaction);
3. determining the type of accounts (i.e. 'asset' or 'liability') and the meaning of the change ('+', '-');
4. specification of the 'debit' and 'credit' sections to be recorded;
5. the preparation of the accounting formula. The recording of economic transactions in the corresponding accounts twice with the same value (amount) - once to the debit of an account and a second time to the credit of the corresponding account is called double-entry bookkeeping. The reciprocal link between the debit of one account and the credit of another account established when recording economic and financial transactions in the current accounts on the basis of double entry is called matching accounts, and the accounts between which such a link is established are called corresponding accounts.

Depending on the changes that economic operations or financial operations in the balance sheet, the correspondence of accounts can be established:

- or only between asset accounts, when changes occur only on the asset side of the balance sheet;
- or only between liability accounts, when the changes occur only on the

- liabilities side of the balance sheet;
- or between accounts on both sides of the balance sheet, when the economic or financial transaction causes changes in both sides of the balance sheet at the same time and in the same amount.

This " principle " **of double-entry bookkeeping**, together with the principle of " balance sheet equality ", is the basis of all accounting, which is why it is also called " double-entry bookkeeping " or " double-entry bookkeeping ".

Depending on the complexity of the economic operation and the number of corresponding accounts, the accounting formulae are:

- *simple formulas* - when only one account is debited and only one corresponding account is credited;
- *compound formulas* - where a single account is debited or credited and several corresponding accounts are credited or debited.

In these complex formulas, the value (sum) recorded is the same.

Summary accounts reflect economic means, sources and processes, in value terms, by groups or categories homogeneous in terms of their content.

For example, the 'Suppliers' account summarises payables to the various economic agents from which materials, raw materials, parts, etc. are purchased. With the help of summary accounts it is possible to know the general, overall situation of a given group of economic resources, sources and processes.

Analytical accounts develop the summary accounts by mirroring the component parts of economic means, sources or processes. The 'Suppliers' account will have analytical accounts with the name of each individual supplier (Agroserv, RAJAC, etc.).

Accounting kept using analytical accounts is called cost accounting. As analytical accounts develop the synthetic accounts, all the rules for the operation of synthetic accounts apply to analytical accounts. Entries are made simultaneously in both the synthetic and analytical accounts so as to ensure consistency between them in terms of balances and turnovers.

The accounts, as a source of information for the management, organisation and conduct of the business of an economic unit, must reflect reality. To this end, accounting uses its own tool for checking compliance with the basic concepts: double entry in the balance sheet and double entry in the accounts, an instrument called the trial balance.

3.4 Trial balance

The trial balance is a table containing: the symbol and name of the accounts used during the management period, the opening balances, the debit and credit balances and the closing balances.

The trial balance is basically a summary table of all the accounts in the general ledger, providing information on opening and closing balances, turnovers and totals at the date of its compilation. It is a tool for summarising the information reflected in the accounts at a given time (month, quarter, half-year, year).

The content and form of presentation of the trial balance may differ depending on:

- a) the type of accounts for which they are prepared:
 - trial balances of synthetic accounts, and
 - trial balance of analytical accounts.
- b) the complexity of the information they contain:
 - single-balance trial balances;
 - trial balances with two ties;
 - trial balances with three ties;
 - four-way trial balance.

The trial balance controls the accuracy of entries in the accounts through the existence of value equalities, namely:

- the total (sum of the original debit balances) equals the total (sum) of the original credit balances, since these totals represent the assets and liabilities of the original balance sheet, which are in the relationship:

$$\sum I. d. b = \sum I. c. b$$

If there is no such value equality, it means that the original balances have been wrongly taken from the balance sheet and the necessary corrections are made;

- the total (sum) of debit turnovers is equal to the total (sum) of credit turnovers, due to double entry in the accounts:

$$\sum D. r = \sum C. r$$

If there is no such value equality, it means that the posting in the accounts has been made incorrectly and the necessary corrections are made;

- the total (sum) of the final debit balances equals the total (sum) of the final credit balances, since these totals represent the assets and liabilities of the final balance sheet, drawn up precisely on the basis of these final balances:

$$\sum F. d. b. = \sum F. c. b.$$

If there is no such value equality, the final balances have been wrongly calculated and the calculations are recalculated.

With all these possibilities for correcting various posting errors in the accounts, the trial balance has this limited function.

In addition to this basic function (control function), the trial balance also performs:

- the function of linking the summary account to its analytical accounts by drawing up analytical trial balances;

- the linking function between the accounts and the balance sheet, by using the balance sheet data (closing balances) when drawing up the final balance sheet;
- the function of grouping, centralising accounting data, recorded over a given period of time, into a single statement providing a wide range of economic information.

The trial balance with two sets of ties is the simplest balance and includes:

- I series: debit and credit turnovers (D.r, C.r.);
- 2nd series: final debit and credit balances (F.d.b., F.c.b.).

As a rule, this balance is drawn up monthly and is called **the turnover balance**.

The three-series **trial balance** is the most commonly used and has, compared to the two-series balance, one more series of ties - initial debit and credit balances (I.d.b., I.c.b.).

- I series: Sid and Sic (initial debit and credit balances);
- 2nd series: D.r. and C.r. (debit and credit turnovers);
- 3rd series: F.d.b. and F.c.b. (final debit and credit balances).

The trial balance with four sets of ties has one more set of ties than the one with three sets - debit and credit amounts (Smd, Smc).

These are calculated:

$$\begin{aligned} \text{Smd} &= \text{I.d.b} + \text{D.r.} \\ \text{Smc} &= \text{I.c.b} + \text{C.r.} \end{aligned}$$

- I series: I.d.b. and I.c.b. (initial debit and credit balances);
- 2nd series: D.r. and C.r. (debit and credit turnovers);
- 3rd series: Smd and Smc (debit and credit amounts);
- 4th series: Sfd and Sfc (debit and credit closing balances)..

The "check" trial balance has the advantage of allowing errors to be detected in the correspondence between accounts.

The trial balance, as indicated above, takes the form of a table in which all the accounts, with their names, used during the period for which it is drawn up are entered first.

The data needed to complete the first two series are then extracted from the accounts, i.e. the initial debit balances are entered in the debit column, the initial credit balances in the credit column, the debit and credit turnover in the respective columns.

Check the accuracy of the data by summing the columns and the existence of the equalities shown, otherwise look for the error and correct it.

Then the final balance is determined for each account (using the formulas shown) and entered in the debit or credit column, depending on whether it is a debit or credit final balance.

The correctness of these calculations is also checked by adding them together and checking that the total amount is equal. If this is not the case, the calculations shall be recalculated until they are correct.

Symbol accounts	Name Accounts	Initial balances		Rulaje		Final balances	
		D	C	D	C	D	C

The trial balance is an extremely useful tool for the accountant, as it can be used to identify various types of errors, such as:

Posting errors in the accounts caused by: failure to comply with the principle of double entry, failure to equalise debit and credit amounts in compound accounting formulas, miscalculation of structural elements of the account and others.

Errors in the compilation of trial balances caused by: incorrectly taking information from the ledger, incorrect addition of columns in the balance, etc. To correct this type of error, the specific trial balance equalities are checked, the scoring operations, by repeating calculations, etc.

CHAPTER 4

ACCOUNTING INFORMATION SYSTEM

4.1 Concept, importance, preparation and processing of accounting documents

One of the procedures of the accounting method is that of documentation, which means that all economic and financial operations affecting the assets must be substantiated and justified by written documents (supporting documents) before being entered in the accounts.

Accounting is characterized by the fact that economic operations are recorded only if they are recorded in supporting documents, known as accounting documents.

The accounting documents are therefore written documents in which economic operations are recorded at the time they are carried out, with the aim of using them as proof that they have been carried out.

The records are a means of linking the three forms of economic recording and form the basis for all subsequent entries and calculations in statistical and accounting records.

By drawing up documents, a control is carried out on the integrity of the assets, the way they are used and kept, the participation in the production activity and the results obtained from this participation. Last but not least, the records are of legal importance and are used as evidence in legal proceedings and in the performance of forensic examinations.

Supporting documents are available to shareholders, auditors, tax authorities and other control bodies to check how the business is conducted and whether the legal provisions on the calculation and payment of taxes and duties are complied with.

- *The structure of the record documents is customized according to the type of operation in question, but there are some mandatory elements, namely:*
- *the name of the document (e.g. invoice, bank statement, receipt, salary statement, consumption voucher, etc.);*
- *the heading containing the name and address of the economic agent who issued the document;*
- *the names of the parties who contributed to the transactions recorded;*
- *the number and date of the document;*
- *description of the economic and financial transactions, sometimes specifying the basis of the legal act on which the record was made;*
- *the signatures of the persons responsible for carrying out economic operations, and of those with preventive financial control functions;*
- *other elements ensuring a complete record of operations in documents.*

The conditions necessary for an accounting document to be considered

valid are as follows: it must be written clearly and legibly, eliminating any controversy or possibility of interpretation, it must not contain erasures or corrections, blank lines must be cancelled, it must be drawn up within the legal deadline, it must contain accurate and true data, the amounts for money values must be written in figures and letters.

4.2 Document classification

In order to standardise and eliminate the inconsistencies related to the use and completion of accounting documents, the Ministry of Finance has drawn up the Nomenclature of models of standardised accounting registers and forms, common in the economy, which do not have a special regime, for financial and accounting activity.

This nomenclature sets out the models and instructions for using the documents.

According to the classification criterion, accounting documents can be classified as follows:

According to the way they are drawn up and their role in the information-decimal system they fulfil within the patrimonial unit, we have:

- supporting documents which provide the input data to the accounting information system and which are drawn up when economic transactions are carried out (e.g. payment order, receipt);
- accounting documents (accounting ledgers) which record and store data in the accounts;
- accounting summary and reporting documents (financial statements) which centralise and transmit information. They serve to aggregate the information contained in the supporting documents, and are drawn up within precise deadlines.

- According to the printing mode, we distinguish:

- standardised documents, the content, form and format of which are standardised by the abovementioned nomenclature. The information contained in them is fixed (repetitive and printed) and variable (completed by each economic operator, depending on the specific nature of the operations recorded). The information may also be broken down into questionnaires (e.g. minutes, statements of account), tables (e.g. salary statements, advance payment lists, etc.), or by grouping (e.g. invoice items).
- untyped documents where the content and form are not predetermined, but are left to the discretion of each asset unit

- According to the use and storage regime, we find:

- special documents for which there is a uniform system of insertion and numbering established by the Ministry of Finance;
- documents without special arrangements for which no strict rules have been laid down, only general rules.

- According to their purpose or function, we distinguish:

- documents ordering the performance of a specific operation (e.g. payment orders);
- mixed (combined) documents which attest both the order and the execution of the operation (examples: cashier's cheque, receipt for payment).

- According to their circuit, we distinguish:

- internal documents circulating only within the establishment;
- external documents which also circulate outside the unit.

- According to their content, we have:

- primary documents, which record information at the time it is produced (e.g.: payment slip);
- centralising documents, which aggregate information from several documents of the same nature and from the same period.

- According to the nature of the assets, we distinguish:

- documents relating to fixed assets;
- documents relating to stocks;
- documents relating to cash assets, etc.

4.3 Supporting documents, basis for accounting entries

The Accounting Act stipulates that any asset transaction is recorded at the time it is carried out in a document which forms the basis of the accounting entries, thus acquiring the quality of a supporting document.

Supporting documents contain various elements, which can be classified into common and specific elements.

One stage prior to entry in the accounts is the *processing of supporting documents*, which involves sorting the documents by operation, combining several supporting documents in a centralised system, and checking the form, substance and arithmetic.

The next step is to *analyze and count* the supporting documents by indicating the symbols of the accounts receivable and payable. Recording is done either document by document or on the basis of a centralizing document which aggregates data in several supporting documents whose contents relate to transactions of the same nature and from the same period.

Failure to draw up, incorrect drawing up and/or failure to use supporting documents in accordance with the methodological rules shall be penalized in accordance with the law.

Entries in the accounts shall be made chronologically by entering the documents in the order of their date of entry or recording and systematically in the accounting ledgers.

Accounting records, other than those required by Article 21 of the Accounting Act No 82/1991, which are drawn up by means of computer

technology, shall be numbered, stamped, initialled and recorded in the records of the establishment.

Archiving of documents is compulsory, according to the legal rules in force. However, they lay down different time limits for keeping documents in the archives. Thus, accounting records and supporting documents must be kept for 10 years, except for salary statements and annual financial statements, which must be kept for 50 years.

Any document issued by an entity must also contain the elements required by the relevant legislation, namely the legal form, tax identification code and share capital, where applicable.

The documents on which the accounting entries are based may be considered as supporting documents only if they provide all the information required by the legal rules in force. Supporting documents which form the basis of accounting entries shall engage the responsibility of the persons who drew them up, countersigned and approved them, as well as those who entered them in the accounts.

Supporting documents arising from transactions/operations for the purchase of goods from natural persons on the basis of a purchase order/trade ledger may be entered in the accounts only if proof is furnished that the goods in question have been received.

The marketing board for agricultural products is regulated by Law No 145/2014 on the establishment of measures to regulate the market for agricultural products.

If the documents relate to expenditure for the provision of services by natural persons imposed on the basis of income rules, in order to be recorded in the accounts, they must be based on contracts or civil agreements concluded for this purpose, as well as the document proving payment.

The financial-accounting documents may be drawn up in another language and another currency, if this is expressly provided for in the accounts, in order to make the appropriate entries in another language and another currency, the following rules shall be observed in the following accounting law, the accounts shall be kept in Romanian and in the national currency. The accounting of operations carried out in foreign currency shall be kept both in national currency and in foreign currency, according to the regulations drawn up for this purpose.

Where financial and accounting documents (supporting documents and accounting documents) are drawn up and entered in the accounts using computerised automatic data-processing systems, the signature is not compulsory. In such cases, procedures must be laid down to identify the persons who initiated, ordered and approved, where appropriate, the operations concerned.

Financial and accounting documents may be submitted in paper or electronic form, provided they are drawn up in accordance with these rules.

A document in electronic format means a document containing the

information required by these rules which has been issued and received in electronic format.

Data shall be entered in documents in ink, in ballpoint pen or by using computerised automatic data processing systems, as appropriate. No erasures, alterations or other such processes shall be permitted in financial and accounting documents, nor shall blanks or missing lines be left between the operations entered therein.

Errors are corrected by crossing out the wrong text or figure by one line, while writing the correct text or figure next to it.

Corrections shall be made on all copies of the document and shall be confirmed by the signature of the person who drew up/drafted the document, stating the date on which the correction was made.

In the case of financial-accounting documents for which corrections are not allowed, such as those on the basis of which cash is received, issued or accounted for, or other documents for which the rules of use provide for such restrictions, the document drawn up in error shall be cancelled and kept or remain in the relevant booklet.

When correcting the supporting document recording the delivery/receipt of tangible assets and fixed assets, confirmation by signature of both the payer and the recipient is required.

The invoice is the supporting document on the basis of which economic transactions are recorded in the accounts.

For economic operations for which, according to the provisions of the Fiscal Code, there is no obligation to draw up an invoice, their recording in the accounts is carried out on the basis of the contracts concluded between the parties and the financial-accounting or banking documents attesting those operations, such as: notice accompanying the goods, receipt, payment/receipt order, bank account statement, accounting note, etc., as appropriate.

In the case of reversals, the number and date of the accounting note reversing the operation shall be mentioned on the initial document and the document, date and serial number of the operation being reversed shall be mentioned in the reversal accounting note.

Entries in the accounts shall be made chronologically, following the sequence of documents according to the date on which they were drawn up or entered in the entity, and systematically, in summary and analytical accounts, in accordance with the rules laid down for each form of entry in the accounts.

The models of the financial and accounting documents may be adapted to the specific needs of the entities, provided that the information content provided for in points 2 and 10 and the rules for their preparation and use are respected. They may be pre-printed or edited using computerised automatic data processing systems. The number of copies of the financial and accounting documents shall be determined by the procedures in accordance with the needs of the entities.

Where the task of drawing up financial and accounting documents is entrusted under a service contract to natural or legal persons, their own internal rules for the drawing up and use of those documents shall be adapted accordingly, and the contract shall contain clauses on the drawing up and use of the forms under those conditions.

Entities may establish their own rules for the preparation and use of financial and accounting documents, provided that they do not contravene the legal regulations in force.

Entities shall ensure an internal numbering system for financial and accounting documents, as follows:

- ✓ the persons responsible for organising and managing the accounts will designate, by written internal decision, one or more persons, as appropriate, to be responsible for allocating and managing the numbers concerned;
- ✓ each document will have a serial number or series, as appropriate, which number or series must be sequential, determined by the entity. The allocation of numbers shall take into account the organisational structure, i.e. managements, working points, branches, etc.

The head of the entity shall, no later than three working days after receipt of the referral, draw up a report including:

- the identification data of the missing documents;
- the name and surname of the person responsible for keeping the documents;
- the date and circumstances in which the documents in question were found to be missing.

The report shall be signed by:

- the head of the entity;
- the head of the compartment.

In the case of the completion of documents using computerised automatic data processing systems, corrections shall be allowed only before processing. The documents presented in the lists of errors, cancellations or additions (on the basis of which changes are made to the entity's files or database) must be signed by persons authorised by the entity's management.

Where financial and accounting documents are processed by third parties (natural or legal persons), in relations between third parties and the beneficiary entities, the supporting documents must be drawn up correctly and on time by the beneficiary entities, which are responsible for the reality of the data entered in the documents.

Where the disappearance of documents is due to the head of the entity himself, the measures provided for in these rules shall be taken by the other members of the board of directors, as appropriate.

Where the lost, stolen or destroyed document was drawn up by the entity in

a single copy, it shall be reconstituted by following the same procedures as the original document, stating on the document's letterhead that it is reconstituted, and shall form the basis of the entries in the accounts.

Whenever the disappearance of documents may constitute a criminal offence, the prosecuting authorities shall be notified immediately.

Documents are reconstructed on the basis of a "reconstruction file".

In order to be recorded in the accounts, economic and financial operations must be supported by original documents drawn up or reconstructed in accordance with these rules. In situations where special regulations require that the original document be kept with another entity, a copy of the document in question shall be used for entry in the accounts.

Any person who discovers that supporting or accounting documents have been lost, misappropriated or destroyed shall, within 24 hours of discovery, inform the head of the entity (the entity's administrator, authorising officer or other person responsible for the management of the entity) in writing of the situation.

If the missing document was issued by another entity, the missing document shall be reconstructed by the issuing entity by making a copy of the existing document at the issuing entity. In this case, the issuing entity shall send the reconstituted document to the requesting entity within 10 working days of receipt of the request. The reconstituted documents must be clearly marked "DUPLICATE", specifying the number and date of the provision on the basis of which the reconstitution was made.

The documents reconstituted in accordance with these rules constitute the legal basis for making entries in the accounts.

Non-nominal expenditure documents (vouchers, non-nominal travel tickets, etc.) lost, stolen or destroyed before being recorded in the accounts may not be reconstructed. The procedure for reconstituting lost, misappropriated or destroyed financial and accounting documents shall be completed within a maximum of 30 days of discovery and, in the event of force majeure, within 90 days of discovery.

If the original document is subsequently found, it shall be cancelled on the basis of an official report and kept together with the report in the recovery file.

Entities are required to keep in their archives the accounting ledgers, other accounting documents and supporting documents on which the accounting entries of economic and financial operations are based.

Supporting documents, accounting records and other financial and accounting documents shall be kept, as the case may be, at the tax domicile, registered office or branch offices, on paper or electronically.

Financial and accounting documents proving the origin of goods with a useful life of more than 5 years shall be kept for the period corresponding to their useful life.

In the event of the cessation of the activity of the companies, the financial-

accounting documents shall be kept in accordance with the provisions of the Companies Act No 31/1990, republished, as subsequently amended and supplemented, or shall be handed over to the state archives, in accordance with the relevant legal provisions, as appropriate.

The archiving of financial-accounting documents in paper format shall be carried out in accordance with the legal provisions and in compliance with the following general rules: financial-accounting documents may be kept, on the basis of service contracts, for a fee, also by economic operators authorised, according to the law, to provide archiving services. The responsibility for keeping financial and accounting documents lies with the authorising officer's administrator or other person responsible for the management of the beneficiary entity.

On the occasion of checks carried out by the competent bodies, the entities must produce, at their request, the documents requested.

The period of retention of the pay slips is 50 years and the period of retention of the registers and other procedures of the entity. In this case, a report is drawn up and the documents removed from the register of the archive are removed from the register.

4.4 Accounting registers

The accounting records, referred to in practice as accounting ledgers, are mandatory for all asset units, ensuring the chronological and systematic recording of operations recorded in the primary documents.

They take various forms: loose sheets, registers, files, computer documents linked in the form of a register, with a content and structure appropriate to the purpose for which they were drawn up.

Depending on the destination or purpose for which they are used, we distinguish: registers for chronological records, registers for systematic records, combined registers.

The chronological records ensure that economic and financial transactions are recorded in the order of the date on which they took place. This category includes the Journal Register, the Receipts and Payments Register, Accounting Notes, etc. The Journal Register is a mandatory register, but under current legislation, Accounting Notes are no longer mandatory registers, as their functions are taken over by the Journal Register.

Systematic record-keeping registers ensure that economic and financial operations are grouped and recorded according to their nature and the date on which they were carried out. In this category we mention: the ledger register, the inventory register, the account sheet for miscellaneous operations, the "master - chess" account sheet.

Combined registers are used for both chronological and systematic recording, as well as for analytical records. This category includes the current journals used in the journal form of accounting.

The Accounting Act and the Regulation on the Application of the Accounting Act stipulate that the main registers to be used are: the Register - Journal, the Register - Inventory and the Ledger. Family associations and natural persons authorized to carry out independent activities may only record asset transactions using the Receipts and Payments Register.

According to the provisions of the accounting law, the mandatory accounting registers are: the Journal Register (code 14-1-1), the Inventory Register (code 14-1-2) and the Ledger (code 14-1-3).

The accounting records shall be used strictly in accordance with their intended purpose and shall be presented in an orderly manner and completed in such a way as to enable the accounting operations carried out to be identified and controlled at any time.

Accounting records may be in the form of registers, loose sheets or computerised listings, as appropriate. The numbering of the pages of the registers shall be in ascending order and the volumes shall be numbered in the order in which they are completed.

The journal register (code 14-1-1) is a mandatory accounting document in which all economic and financial transactions carried out by the entity are recorded chronologically. Transactions of the same nature carried out at the same place of activity (workshop, department, etc.) may be summarised in a centralising document, known as a subsidiary journal, which forms the basis for the entry in the journal register.

Entities may use auxiliary journals for: cash and bank operations, settlements with suppliers, the situation of receipt and payment of invoices, etc.

The entries in the Journal Register must include details of: the type, number and date of the supporting document, explanations of the operations concerned and the summary debit and credit accounts in which the amounts corresponding to the operations carried out have been recorded.

Entities using subsidiary ledgers may record in the Journal Register centralised amounts per account, taken from liabilities and own capital entered in the Inventory Register on the basis of inventory lists or other documents justifying the nature of these items existing at the end of the financial year.

Where the inventory is taken during the year, the balances existing at the date of the inventory shall be entered in the inventory ledger, to which shall be added the entries and subtracted the withdrawals from the date of the inventory up to the end of the financial year.

The general ledger (code 14-1-3) is a mandatory accounting document in which the movement and existence of all assets, liabilities and equity at a given time is recorded monthly and systematically by grouping the accounts. It is a summary and systematic accounting document and contains the account symbol and the corresponding accounts (debit or credit), the debit and credit turnover and the account balance.

The General Ledger Register may contain one tab for each summary account used by the entity.

This ledger forms the basis for the trial balance.

The General Ledger Register may be replaced by the Account Sheet for miscellaneous transactions.

The listing of the ledger register shall be carried out at the request of the control bodies and for the needs of the entity.

The accounting records required for persons who keep accounts on the basis of the rules of single-entry bookkeeping.

Natural persons carrying out income-producing activities, as defined by the Fiscal Code, whose income is determined in the real system and who keep accounts on the basis of the rules of single-entry bookkeeping, shall draw up the Register - Receipts and Payments Journal (code 14-1-1/b) and the Register - Inventory (code 14-1-2/b), regulated by Order of the Minister of Public Finance No 170/2015 approving the accounting regulations on single-entry bookkeeping.

The persons referred to in Article 2(a) of the Order of the Minister of Public Finance No 170/2015 approving the Accounting Regulations on single-entry bookkeeping and opting to keep accounts on the basis of the double-entry bookkeeping rules shall draw up the Journal Register (code 14-1-1) and the Inventory Register (code 14-1-2). The preparation, editing and keeping of accounting records and other financial and accounting documents shall be carried out in accordance with these rules.

The main forms of recording in the accounts of economic and financial operations for units which carry out double-entry bookkeeping are: "on journals", "master-book" and the combined form "master-book with journals".

Under the "journal" form of accounting, the main registers and forms to be used are:

- Register - journal (code 14-1-1);
- Inventory register (code 14-1-2);
- General ledger (code 14-1-3);
- subsidiary journals;
- Trial balance.

The logbook (code 14-1-1) is used for the chronological recording of all economic and financial operations recorded in the supporting documents. For operations not based on supporting documents, the Accounting Note (code 14-6-2/A) is to be drawn up.

Accounting notes are based on supporting notes or calculation notes and are recorded chronologically in the Journal Register.

Entities may use auxiliary journals by type of transactions, such as: cash and bank transactions, transactions relating to settlements with suppliers, the cash receipt/payment status of invoices, transactions relating to wages and social security contributions, social protection of the unemployed and health insurance, other transactions.

Monthly or at such other period as may be prescribed by law, the totals of the amounts receivable or payable recorded during the month (period) shall be established in each subsidiary journal and entered in the Journal Register.

Analytical accounts may be kept either directly on these journals (for some accounts) or using other common forms (analytical account sheet for tangible assets, account sheet for miscellaneous operations, etc.) or specific forms used for this purpose.

Journal entries shall be made chronologically throughout the month (period) or only at the end of the month (period), either directly on the basis of supporting documents or on the basis of centralising documents drawn up for the operations relating to the month (period) in question, which shall be recorded chronologically therein.

The general ledger (code 14-1-3) is the accounting system document which contains all the summary accounts and reflects, at a given time, the existence and movement of all assets, liabilities and equity. The general ledger is used to establish the monthly turnovers and balances of the accounts and forms the basis for the balance sheet.

CHAPTER 5

ACCOUNTING FINANCIAL STATEMENTS

5.1 Generalities

The annual financial statements are "official documents presenting the economic and financial situation, which must give a true and fair view of the financial position, financial performance and other information relating to the business".

The purpose of the accounts is to reflect in monetary terms the movable and immovable property, cash assets, securities, rights and obligations of the trader, as well as the movements and changes resulting from the transactions carried out, expenditure, income and the result obtained by the trader.

Under the law, the annual financial statement is the official management document of the trader. It must give a true, clear and complete picture of the trader's assets, financial situation and results.

According to the Accounting Regulations harmonised with the European Economic Community Directives and International Accounting Standards, approved by order of the Minister of Public Finance, the annual financial statements consist of:

- + Balance sheet;
- + The profit and loss account;
- + Statement of changes in equity;
- + Cash flow statement;
- + Accounting policies;
- + Explanatory notes.

The term '*annual financial statements*' is taken from International Accounting Standards. In the Fourth Directive of the European Economic Community, annual accounts mean the balance sheet, profit and loss account and explanatory notes.

As a set of summary documents, the annual financial statements must give a true, fair and comprehensive view of the assets, liabilities, financial position and profit or loss of the patrimonial unit.

The annual financial statements are mandatory, including in the event of a merger, division or cessation of activity, in accordance with the law. For autonomous companies, commercial companies and national companies in which the State holds at least 20% of the share capital, as well as for other legal entities, the Ministry of Public Finance may establish the preparation and submission of financial statements also at other periods than those mentioned, within the financial year.

Companies classified by special regulations as micro-enterprises apply specific accounting rules, approved by order of the Minister of Public Finance, and

the financial statements consist of a balance sheet and a profit and loss account. The annual financial statements must be accompanied by the directors' report. In the case of public institutions, financial statements are drawn up quarterly and annually and consist of a balance sheet, budget outturn account and annexes.

The financial year begins on 1 January and ends on 31 December. The exception occurs in the first year of activity, when it begins on the date of establishment or registration of the legal entity with the Trade Register, as provided by law. On a proposal from the Ministry of Public Finance, the Government may approve that the financial year begins and ends on dates other than those specified above.

The preparation of the annual financial statements must be preceded by a general inventory of assets and liabilities and other assets and values under management and administration, in accordance with the rules issued for this purpose by the Ministry of Public Finance.

After the annual financial statements have been drawn up (including those drawn up on the occasion of a merger, division or cessation of activity), they shall be subject to a financial audit, which shall be carried out by financial auditors, natural or legal persons authorized by law.

Annual financial statements are kept for 50 years. In the event of cessation of activity, the statements, together with the books and other documents, shall be handed over to the State archives, in accordance with the relevant legal provisions.

The financial statements shall be drawn up in three copies. In order to provide information to the State's institutional system, one copy shall be submitted to the General Directorate of Public Finance of the counties and the municipality of Bucharest, respectively, within the time limits provided for by law. Public institutions and other legal entities whose managers are authorizing officers shall submit a copy of the quarterly and annual financial statements to the superior hierarchical body within the deadlines set by the latter.

Ministries, other central government bodies, public authorities and administrative-territorial units whose heads are chief authorizing officers shall submit to the Ministry of Public Finance a copy of the quarterly and annual financial statements in accordance with the rules and within the time limits laid down by the Ministry.

The annual financial statements must give a true and fair view of the financial position, performance, changes in equity and cash flows of the undertaking for the financial year in question.

5.2 Form and content of company financial statements

The format required for the balance sheet must include at least the following items:

A. Non-current assets

I. Intangible assets

1. Formation expenses (when regulations allow their immobilisation);

2. Development costs (when regulations allow for capitalisation);
3. Concessions, patents, licences, trade marks, similar rights and values and other intangible fixed assets (acquired against payment or created by the company);
4. Purchased goodwill;
5. Advances and intangible assets in course of construction.

II. Tangible assets

1. Land and buildings;
2. Technical installations and machinery;
3. Other plant, machinery and furniture;
4. Advances and tangible fixed assets in course of construction.

III. Financial assets

1. Equity interests held in group companies;
2. Claims on group companies other than trading companies;
3. Securities in the form of participating interests;
4. Receivables from participating interests;
5. Securities held as fixed assets;
6. Other claims;
7. Own shares (with indication of nominal value in the notes)..

B. Current assets

I. Stocks

1. Raw materials and consumables;
2. Production in progress;
3. Finished products and goods;
4. Advances for stock purchases.

II. Receivables (amounts to be collected after more than one year are shown separately for each item)

1. Trade receivables;
2. Amounts receivable from group companies;
3. Amounts receivable from companies in which participating interests are held;
4. Other receivables;
5. Claims relating to subscribed and unpaid capital.

III. Short-term financial investments

1. Equity interests held in group companies;
2. Own shares (with indication of par value in the notes);
3. Other short-term financial investments.

IV. House and bank accounts

C. Advance expenses

D. Debts to be paid within one year

1. Borrowings from bond issues, showing separately borrowings in convertible currencies;
2. Amounts owed to credit institutions;
3. Advances received on account of orders;

4. Trade debts;
5. Trade bills payable;
6. Amounts due to companies within the group;
7. Amounts due in respect of participating interests;
8. Other liabilities, including tax and social security liabilities.

E. Net current assets and net current liabilities

F. Total assets minus current liabilities

G. Debts to be paid in more than one year

1. Loans from bond issues, showing separately loans in convertible currencies;
2. Amounts owed to credit institutions;
3. Advances received on account of orders;
4. Trade debts;
5. Trade bills payable;
6. Amounts due to companies within the group;
7. Amounts due in respect of participating interests;
8. Other liabilities, including tax and social security liabilities.

H. Provisions for risks and charges

1. Provisions for pensions and similar obligations;
2. Other provisions.

I. Income in advance

J. Capital and reserves

I. Subscribed capital (showing paid-in and paid-up capital separately)

II. Capital premium

III. Revaluation reserves

IV. Reserve

1. Legal reserves;
2. Reserves for own shares;
3. Statutory or contractual reserves;
4. Other reserves.

V. Reported result

VI. Result for the financial year

A company's balance sheet and profit and loss account may be expanded with any asset or liability, income or expense, which is not provided for in the adopted format. However, their structure cannot be changed from one financial year to the next. Derogations are allowed only in exceptional cases, but any derogation must be disclosed in the explanatory notes together with the reasons for it.

Items in the balance sheet and profit and loss account shown with Arabic numerals may be aggregated into a single item in the financial statements of an undertaking if:

- a) the individual amounts are not material to the assessment of the financial position and performance of the enterprise for the financial year;
- b) aggregation improves clarity of presentation; the individual amounts of any items combined in this way will be disclosed in the explanatory notes.

Where the amounts for the current and previous financial year shown in the balance sheet and profit and loss account are not comparable, the amounts for the previous financial year must be restated accordingly to ensure comparability. The results of the restatement, the reasons for it and how it was made should be disclosed in the explanatory notes.

5.3 Balance sheet regulations

The balance sheet has entered the world of economic theory and practice as a model for synthesising at a given time, in monetary terms, the relations of balance between the assets and liabilities of the patrimony, seen in its totality and structurality, its basic function being to establish the situation of the patrimony. Subsequently, its function and content were broadened to include the evaluation of the financial result as a component element of the balance sheet.

The concept of the balance sheet as a model for calculating and describing the assets and liabilities situation is the one most commonly used in the literature. Today, the balance sheet is taking on new meanings, being analysed and promoted as a model for representing the situation, the movement and the transformation of assets. The balance sheet has been conceived and structured as a set of models, and is also referred to as the 'general heritage account'.

The balance sheet is the summary accounting document showing the assets (grouped by nature, purpose and liquidity) and liabilities (grouped by nature, source and due date) of the enterprise at the end of the financial year and in the other situations provided for by law. The information relating to assets and liabilities shown in the balance sheet relates to the previous and current financial year and is presented in the form of the summary account balances at the end of the financial year.

Where an asset or liability is related to more than one other balance sheet item, its relationship to the other items should be disclosed either under the item under which it appears or in the explanatory notes if its disclosure is essential to an understanding of the annual accounts.

Own shares and shares held in subsidiaries should be shown separately under the headings provided for them.

All commitments in the form of guarantees, endorsements and mortgages of any kind, if they qualify for recognition in the balance sheet as assets or liabilities, must be clearly disclosed in the notes. For any significant guarantees that have been given, a detailed disclosure must be made, distinguishing between the

various types of guarantees recognised by Romanian law and those which are not recognised by Romanian law.

For each item disclosed under Fixed assets, the following information must be given in the explanatory notes:

- the corresponding values of the item at the beginning and end of the financial year;
- movements due to changes in value during the year, additions, disposals and transfers.

The values for the elements will be determined on the basis of the following criteria:

- acquisition cost;
- production cost;
- any other of the following criteria: historical cost, revaluation of tangible fixed assets in accordance with the legal regulations in force, valuation by methods designed to take account of inflation, the usefulness of the asset, its condition and the market price, excluding depreciation and provisions for impairment.

For each fixed asset the following shall be presented:

- the amount of accumulated depreciation and provisions for impairment at the beginning and end of the year;
- the amount of accumulated depreciation and provisions for impairment relating to that financial year;
- the amount of adjustments made in respect of depreciation and provisions for impairment during the year as a result of disposals of fixed assets;
- the amount of adjustments made to depreciation and provisions for impairment in respect of previous years.

If in the first financial year of application of these regulations the acquisition cost or production cost of an asset is not known and there is no price or cost information necessary to determine it, or if such information cannot be obtained without undue expense or delay, the acquisition cost or production cost shall be the fair value attributed to the asset. This will be disclosed at the beginning of the financial year.

Rights to fixed assets and other similar rights will be shown under the appropriate balance sheet items.

Expenditure incurred during the financial year but relating to a subsequent financial year will be shown under the balance sheet item 'Prepaid expenses'. Accrued income is shown under 'Receivables'.

Revenue recognised before the year-end date but relating to a subsequent financial year shall be shown under 'Revenue in advance'. Expenditure incurred shall be entered under 'Liabilities'.

A provision will only be recognised when:

- an enterprise has a present obligation (legal or constructive) arising from a past event;

- it is probable that an outflow of resources affecting economic benefits will be required to settle the obligation.

Analysed through the prism of modelling theory, the balance sheet is a structural model of assets and liabilities as a multitude of the assets of a management unit. In the asset side of the balance sheet, the elements are structured as follows:

a) Fixed or fixed assets, also referred to as long-term assets, are acquired with a view to their durable use. They are associated with the investment decision and take the form of assets of any kind, whether movable or immovable, tangible or intangible, acquired or created by the undertaking and intended to serve the activity of the asset unit over a long period of time.

- - Intangible fixed assets comprise those economic investment values which do not physically take the form of tangible fixed assets.

About:

- formation expenses, which are expenses incurred in setting up or developing the unit, and merger expenses. They include: fees and charges for registration and incorporation; expenses relating to the issue and sale of shares; market research and advertising expenses; expenses incurred in carrying out research work or objectives. It is amortised over a maximum of five years.

- Concessions, patents, licences, trademarks and other similar rights comprise all expenditure incurred for the amortisation of rights to exploit a good, activity or service. Depreciation of such expenditure is charged over the period during which the enterprise has acquired the right to exploit or use such assets.

- goodwill is that part of the goodwill which is not included in the other assets, but which contributes to the maintenance or development of the company's business potential, such as: clientele, goodwill, outlets, reputation.

- Tangible fixed assets (tangible fixed assets or tangible fixed assets) are tangible assets of long-life use used in the activity of an enterprise. They constitute the substance of an enterprise, its industrial or commercial tool, and are made up of land and fixed assets (buildings, machinery, equipment, plant and means of transport, etc.). If the tangible goods purchased or created are not finished, they are included in the category of fixed assets in course of construction or investments in course of construction.

- Financial fixed assets (financial or portfolio investments) comprise financial assets invested by the enterprise in the assets of other companies in the form of: participating interests, other financial fixed assets, debt securities attached to participating interests, loans granted and other financial fixed assets.

- equity securities are securities in the form of shares or stocks invested by the asset holder in the capital of other asset units. The holding of these securities enables the exercise of a certain influence or control over the management of the companies issuing them.

- portfolio investment securities are acquired by the asset unit with a view to generating financial income, without being able to intervene in the management of the issuing asset unit.

- non-current assets consist of: receivables related to participating interests, long-term loans and other non-current assets.

b) Current assets are all the assets and liabilities necessary for the operating cycle. They are not intended to remain permanently with the undertaking, with the exception of those items relating to the specific features of the manufacturing process.

Stocks are all goods and services that occur during the operating cycle either to be sold in the same condition or at the end of the production process, or to be consumed when first used.

Receivables are potential short-term rights of the enterprise arising from relations with various natural or legal persons realisable at certain times. These rights may arise from relations with customers or from non-commercial relations with staff, the State, associations or other debtors.

Cash and cash equivalents are cash and cash equivalents and investments are securities purchased by the enterprise for the purpose of realising a capital gain or income in the short term.

c) Prepayments and accrued income and similar accounts consist of: prepaid expenses, translation differences and bond redemption premiums.

Bond redemption premiums are capitalised financial charges.

The liabilities side of the balance sheet reflects the sources of financing of the enterprise.

Own capital (net assets) represents the assets and liabilities belonging to the owners of enterprises, which are not due at the end of the financial year.

Operational categories in the financial analysis:

- equity is determined at the year-end before the profit is distributed;
- the net position determined after profit distribution by adding together the items: share capital, share-related premiums, revaluation differences, reserves and retained earnings;
- the adjusted net assets resulting from the correction of the book net assets by unrealised gains or losses.

Equity capital comprises:

- share capital is the nominal value of the shares or units, i.e. the contribution in kind or in cash;
- capital-related premiums refer to share premium, contribution and merger premiums, which are sources generated by operations to increase share capital;
- revaluation differences are equal to the balance between the (higher) present value and the (lower) recorded value of the revalued asset, which is transferred either to share capital or to reserves;

- reserves are the result of capitalisation of profits and are made up of: legal reserves, statutory reserves and other reserves.
- Foreign capital is made up of the debts of the legal entity, whether short-term or long-term. They are recorded in the accounts at nominal value.
- Short-term liabilities are amounts payable within a period of up to one year. This category includes debts to suppliers, tax and social security debts (health, unemployment, social security funds), short-term loans.
- Long-term debts are amounts to be paid over a period of more than one year. This category includes medium- and long-term bank loans.
- Provisions for risks and charges are made for litigation, fines, penalties, compensation, damages, other doubtful debts, service charges during the guarantee period and other charges relating to guarantees given to customers.

5.4 Compilation of financial statements

A complete set of financial statements includes the balance sheet, income statement, statement of changes in equity, cash flow statement and notes. IAS 1 provides practical guidance on going concern, accruals, permanence and materiality.

Many jurisdictions prescribe in legislation that the responsibility for preparing financial statements rests with directors and/or management. IAS 1, paragraph 6 clarifies that the responsibility for the preparation and presentation of financial statements in accordance with IAS rests either with the board of directors or other management body.

To be credible, financial statements must meet a number of qualitative characteristics:

- faithful representation;
- the prevalence of economic over legal;
- neutrality;
- prudence;
- completeness.

Fair presentation is normally achieved if users obtain information that is consistent with the economic reality on which it is based and if they are informed of the material uncertainties associated with the recognition and measurement of items presented in the financial statements. These should be disclosed in the notes. Accounting should reflect the economic substance of the transaction and not just its legal form.

Prevalence of the economic over the legal - for information to present credibly the events and transactions it represents, it is necessary that they are accounted for and presented in accordance with their substance and economic reality, and not just their legal form, the substance of transactions or other events not always being consistent with what is apparent from their legal or conventional form.

Completeness means that the information is complete within reasonable limits of materiality and the cost of obtaining that information.

IAS 1, paragraph 38 requires the presentation of comparative numerical information at least for the prior period, unless other Standards permit or require otherwise.

IAS 1, paragraphs 42 to 52, contain some general requirements for financial statements. These include the identification of the statements (balance sheet, cash flow statement, etc.), the name of the reporting enterprise, the reporting currency, the balance sheet date and the accounting period, and any changes to these during the period. These provisions are very clear and there should be no difficulties in interpreting or applying them. IAS 1, paragraph 52 encourages companies to publish annual financial statements within six months of the balance sheet date. Even where this is not a legal requirement, financial statements should be published within this period.

IAS 1 does not require the use of a standardised (categorised) balance sheet, as such an approach is substantially influenced by the business in which the company operates. In practice, most commercial or industrial enterprises whose operations involve a high turnover of assets and liabilities present a categorised balance sheet (distinguishing between working capital and non-current items) because a significant part of the assets and liabilities of that company will be realised over a well-defined operating cycle, e.g. 12 months. Other companies, such as real estate companies, by comparison have a longer operating cycle, in which case they are not expected to realise or extinguish their assets and liabilities over a period of only 12 months. Such enterprises often do not present a balance sheet broken down by category.

Other enterprises, such as investment companies and mutual funds, have assets and liabilities that can be realised almost immediately or extinguished in a short period of time and can be measured using fair values. In these businesses, the realisation of assets and the extinguishment of liabilities is largely dependent on fluctuations in market value and therefore the distinction between current and long-term items is not considered meaningful - indeed, this is at odds with the way the business is run.

IAS 1, paragraphs 57 to 65 apply only to the financial statements of companies that present current or non-current assets and liabilities as separate categories in the balance sheet. Items are classified as current if they are used within one operating cycle or are expected to be realised within 12 months of the balance sheet date. Deciding whether an item is involved in the operating cycle may require some degree of professional judgement, but is not intended to create a need for a choice between the operating cycle and the 12-month period.

Regarding the presentation of balance sheet items, IAS 1 adopts a three-step approach:

- (a) Minimum (mandatory) presentation requirements - IAS 1 paragraph 66 prescribes the minimum mandatory balance sheet structure;

- (b) Detailed (judgement-based) presentation - IAS 1 paragraph 67 requires the presentation of additional separately disclosed items, headings and subtotals in the balance sheet which, under paragraph 70, will be required in most cases;
- (c) Sub-classification (classification is optional, based on judgement).

The standard does not include a standard balance sheet format. Therefore, management may use professional judgment regarding presentation in most cases, such as whether to use a horizontal or vertical format for the balance sheet, how detailed the sub-classifications are to be, and except for certain minimum requirements imposed, what information is to be presented in the balance sheet and what information is to be presented in the notes. Although there is no requirement to present balance sheet items in a particular order, paragraph 53 of IAS 1 requires that items should be presented 'broadly' in the order of their liquidity. This creates the alternative of ordering balance sheet items either from current and liquid or vice versa, both of which are used in practice and considered appropriate.

Detailed structure

The minimum structure should be detailed by presenting additional items, categories or subtotals in the balance sheet where required by another Standard or where such presentation is necessary for the fair presentation of the financial position of the enterprise. For example, IAS 30 'Presentation in the Financial Statements of Banks and Other Financial Institutions', provides specific requirements for such undertakings. Any disclosures that require additional detail to that already made may be reported in the notes (e.g. highlighting the different classes of inventories in accordance with paragraph 34(b) of IAS 2).

IAS 1, paragraph 70 suggests that reliance on professional judgement may lead to additional separate disclosures. Consideration of the 'nature, liquidity and materiality of assets', the 'function' of assets and the 'amount, nature and duration of liabilities' will often result in separate disclosure of current and long-term assets and liabilities;

- monetary and non-monetary assets and liabilities;
- operating and financial assets and liabilities;
- interest-bearing and non-interest-bearing provisions and liabilities.

For example, due to their different nature, goodwill and other intangible assets will usually be presented separately on the balance sheet, although this is not required by IAS 1.

IAS 1, paragraph 71 states that assets and liabilities that differ in nature or function are sometimes measured on different bases (e.g. classes of land and fixed assets measured at cost or fair value in accordance with IAS 16). This paragraph states that the use of different measurement bases requires separate disclosure. Where assets have the same nature and function (for example, classes of inventories measured using different cost formulas in accordance with IAS-1), this information may be disclosed in footnotes.

5.5 Results account

If the balance sheet expresses the balance sheet at the end of a financial year, the profit and loss account reflects how that balance sheet was arrived at, what were the income and expenditure flows that determined the trajectory of the company's development.

The profit and loss account provides information on the production, marketing and financial activity of the company and comprises:

- turnover;
- income and expenditure grouped by nature and classified by three types of activity: operating, financial and exceptional;
- the results (profit or loss) generated by the three activities;
- gross result for the year, income tax and net result.

The operating (core) activity refers to the industrial, investment, commercial and service sectors; the financial activity refers to holdings in the capital of other companies and other money and financial market investments, together forming the day-to-day business of the enterprise. Exceptional activity generates a range of income and expenditure from the firm's exceptional management and capital operations.

Operating income comprises:

- Turnover, the sum of revenue from the sale of goods and revenue from production sold;
- stored production (from the change in stocks and the balance of invoices relating to stored production);
- fixed production;
- operating subsidies;
- income from the release of provisions which have not been used;
- other operating income.

Operating expenses relate to:

- the cost of the goods purchased;
- expenditure on the supply of raw materials, materials and changes in material stocks;
- expenditure on work and services carried out by third parties;
- taxes, duties and similar charges (excluding corporation tax);
- payment of salaries and social security costs;
- depreciation of fixed assets;
- provisions for current assets and for operating risks and charges;
- other operating expenses.

Operating income and expenses determine the size of the operating result (profit or loss).

Financial income comes from:

- the company's participation in the capital of other companies;
- income from fixed investments;

- interest subsidised by banks on cash in the account;
- favourable exchange rate differences;
- reversal of financial provisions set up but not used;
- income from the sale of investment securities.

Financial expenditure includes:

- interest and commissions paid to banks and other third party creditors;
- depreciation and financial provisions calculated;
- unfavourable exchange rate differences;
- charges relating to the disposal of investment securities.

Financial income and expenses determine the size of the financial result (profit or loss).

The size of the operating result and the financial result determine the current result.

Exceptional income comes from:

- management operations:
 - fines, penalties imposed on third parties;
 - damages;
 - tax relief (reductions, exemptions)..
- capital transactions:
 - proceeds from the disposal of assets;
 - investment grants transferred to revenue;
 - reversals of provisions.

The exceptional expenditure comes from:

- management operations:
 - fines, penalties, compensation paid to third parties;
 - donations granted.
- capital transactions:
 - book value of stolen, destroyed, lost assets;
 - depreciation and exceptional provisions calculated.

Exceptional income and expenses determine the size of the exceptional result (profit or loss). The size of the current result and the exceptional result determine the gross result for the year. It can also be calculated on the basis of total income and expenditure, i.e. the results for the three activities. Deducting corporation tax from the gross result gives the net result for the year (profit or loss). Corporation tax is applied to the taxable profit which is obtained from the total profit, less non-taxable income, then adding the non-deductible expenses for tax purposes specified by law.

5.6 Annex to the balance sheet. Management report

The annex to the balance sheet is a summary accounting document which contributes to a true and fair view of the annual accounts. It takes the form of a set of financial statements containing supplementary and explanatory information in

relation to the balance sheet and the profit and loss account, as well as a presentation in the form of a text on the accounting rules and methods used.

The management report is the balance sheet document used for the analytical interpretation of the assets and liabilities situation, i.e. the evolution of the financial situation and the result. It is used to provide balance sheet information on the assets and liabilities situation and its foreseeable development; significant events in the activity of the asset unit after the end of the financial year; holdings in the capital of other units; the activity and overall results of its branches and sub-units; research, development and other references to the activity carried out which are considered necessary for inclusion in the management report.

At the same time, the management report responds to the information needs of business partners outside the enterprise, economic units or financial-banking institutions, in order to base possible cooperation actions with the enterprise in question.

Situation of changes in equity

The statement of changes in equity is a separate component of the company's financial statements, showing in detail all changes in equity during a financial year. On the basis of the information provided by this document, it is possible to analyse the capital maintenance capacity and the profit or loss of the undertaking.

The statement of changes in equity should show:

- ✓ net profit or loss for the period;
- ✓ each item of income or expense, gain or loss that is recognised directly in equity and the total of those items;
- ✓ the cumulative effect of changes in accounting policies and the correction of fundamental errors.

Companies must disclose either in the statement of changes in equity or in the explanatory notes:

- capital transactions with and distributions to owners;
- the balance of accumulated profit or loss at the beginning of the period and at the balance sheet date and changes during the period;
- a reconciliation between the carrying amount of each category of equity at the beginning and end of the period, showing each change separately.

Cash flow statement

The cash flow statement is a useful financial document in explaining the changes in the company's assets during the year, providing information on how financial resources have been financed and used.

The cash flows are analysed according to the nature of the business:

- operating;
- investing;
- financing.

Explanatory notes

The explanatory notes contain additional information relevant to the needs of users in terms of financial position and results achieved. They should be presented in a systematic manner, with each significant balance sheet item being accompanied by a reference to the note containing information relating to that item.

The following explanatory notes will be presented in the financial statements:

1. Fixed assets
2. Provisions for risks and charges
3. Allocation of profit
4. Analysis of operating result
5. Statement of receivables and payables
6. Accounting principles, policies and methods
7. Shares and bonds
8. Information on employees, directors and officers
9. Examples of calculation and analysis of main economic and financial indicators
10. Other information.

Report of the administrators

The Board of Directors shall draw up a report for each financial year, which shall contain:

- an accurate analysis of the development of the undertaking's activities during the financial year and of its situation at the end of that year;
- the amount of the proposed dividend;
- information on significant events affecting the undertaking;
- information on the probable development of the company's business;
- information on research and development activities;
- information concerning the shares; the name and professional qualifications of each director;
- environmental protection policy.

This report shall be approved by the Board of Directors and must be signed by its Chairman.

CHAPTER 6

FINANCIAL POSITION OF THE COMPANY

In order to cope with a competitive environment, the strategic objective pursued by a company is often to maximise its value. This can only be achieved under conditions of sound financial balance and superior profitability. It is also important to optimise financial flexibility while maintaining liquidity and solvency.

With these criteria in mind, managers and capital providers calculate capital structure ratios based on the company's balance sheet, which allow the balance sheet structure to be compared over time and space.

At the asset level, the most important indicators include the non-current assets ratio, the intangible assets ratio, the tangible fixed assets ratio, the financial fixed assets ratio, the current assets ratio, the inventories ratio, the receivables ratio and the cash and short-term financial investments ratio.

Rate of tangible fixed assets

The tangible asset ratio (R_{ic}) shows the share of tangible assets in total fixed assets and measures the ability of enterprises to withstand a crisis, to adapt to sudden changes in technology or market requirements.

Current assets rate

Current assets ratio (CAR) is the ratio of current assets to total assets.

The current assets ratio is an indicator whose value depends on the sector of activity, the length of the cycle of circulation of goods, the collection period of receivables and the existence of liquid assets.

The stock ratio (R_{st}) reflects the share of the least liquid current assets in total current assets. This ratio takes different values being influenced by the sector of activity, the length of the operating cycle, cyclical factors and market conditions.

The receivables ratio (R_{cr}) reflects the commercial credit policy, "expressing the portfolio of receivables in the unit's assets and the size of the settlement term granted to customers", as well as the management of the company's financial resources.

The receivables ratio (R_{cr}) shows the share of receivables that the firm has in total current assets. This ratio is primarily influenced by the object of activity

The liquidity ratio (LR) characterises the degree of liquidity of the asset, its informational value, becoming important for the dynamic analysis of the treasury and financial situation over several financial years.

The liability structure ratios show how the sources of funding are structured according to their source and the extent to which they are due. The level of these ratios can be used to identify the existence or non-existence of an adequate financial structure, the result of the policy promoted by the unit's management.

The financial stability ratio (R_{sf}) reflects the extent to which the firm has permanent financial resources in relation to total resources. The share of permanent capital in financial resources reflects the permanent nature of the financing of the business, providing a high degree of security through stability in financing.

Analysis of current funding level

The current resource ratio (CRR), that is the degree of current financing, reflects the extent to which current resources participate in the formation of total resources and activities

Financial self-sufficiency highlights the extent to which sources of finance belong to the owner. The higher the share of own sources in total sources of finance, the higher the financial autonomy of the enterprise.

The overall financial autonomy ratio (AFR) shows how much of the firm's assets are financed from own resources

Financial autonomy is essential for a business because it gives it the freedom to decide and to find and take out new loans.

Leverage ratios express in relative magnitudes the level of debt the firm has in relation to either total sources of finance or own resources alone.

The overall indebtedness ratio (RIR) compared the total debt owed by the firm to its creditors.

Liquidity measures a firm's ability to meet short-term obligations and involves the ability to quickly turn current assets into cash.

Liquidity indicators are calculated as the ratio of current assets.

In the literature, liquidity ratios are also known as cash flow ratios and are used to measure a firm's ability to pay.

Analysing the ratios resulting from comparing the total potential liquidity with potential liabilities is a quick and easy method of assessing the extent to which the enterprise is meeting its short-term obligations.

In practice, the following indicators are used:

a) Current liquidity ratio (overall liquidity) represents the ability of current assets to meet the current liabilities of the enterprise:

➤ $\text{Current liquidity ratio} = \frac{\text{current assets}}{\text{current liabilities}}$

b) Intermediate (reduced) liquidity ratio shows the ability of current assets less inventories to meet the enterprise's current liabilities:

➤ $\text{Intermediate liquidity ratio or acid test} = \frac{\text{current assets} - \text{inventories}}{\text{current liabilities}}$

c) The immediate (effective) liquidity ratio measures the extent to which the treasury covers current liabilities:

Solvency is the firm's ability to meet medium and long-term maturities and depends on the size of its medium and long-term liabilities.

Solvency is the result of the balance between cash receipts and cash payments.

Solvency reflects the firm's ability to pay its outstanding debts from available resources and expresses the "ability of the firm to meet medium and long-term payments when they fall due".

Solvency is assessed by comparing the liquidity of the assets and the liabilities on the balance sheet and by using liability structure ratios that characterise the firm's indebtedness and financial autonomy..

The following indicators are used for solvency analysis

Net accounting assets (NAA)

$NAA = \text{Total assets} - \text{Total liabilities}$

This indicator gives a picture of the overall solvency of the firm and the size of its equity capital, providing a cushion for creditors in the event of adverse developments in the firm's business.

➤ *Overall solvency ratio (Rsg)*

$Rsg = \text{Total assets} / \text{Total liabilities}$

This indicator "shows the extent to which the firm's total assets can cover its total liabilities", and the value of this indicator becomes important for the firm's creditors because it is the guarantee of the firm's net assets.

➤ *Total debt ratio (Rd)*

$Rd = \text{Total debt} / \text{Equity}$

This indicator expresses the firm's level of debt coverage from equity.

➤ *Debt capacity (Cd)* expresses the ratio of equity to permanent capital.

Financial equilibrium rates

The general rule in achieving and maintaining the financial equilibrium of the company is to cover fixed assets and part of the current assets from the permanent capital of the company. The financial equilibrium of the company can be considered both as a permanent and an absolute imperative for any economic agent

Thus, the analysis of financial balance on the basis of the balance sheet can be carried out on three levels:

1. long-term (through working capital),
2. short-term (working capital requirements)
3. current balance (cash flow)

Working capital is "the surplus of permanent resources that can be used to cover or finance current assets after the net fixed assets have been fully financed" Based either on the elements contained in the balance sheet or in the functional balance sheet, the analysis of working capital must be carried out with care, taking into account its trend, the period of time, information on the branch of activity and the definition of a "normal" level of NFR for each company.

The working capital requirement is calculated as the difference between the financing needs of the operating cycle and their sources of financing

If the NFR is positive, there is a surplus of temporary needs over current sources of funding, and vice versa. The NFR analysis is carried out taking into account investment policy, asset turnover and suppliers

In terms of treasury analysis, it can be categorised as positive ($T > 0$, $FR > NFR$), negative ($T < 0$, $FR < NFR$), or accidentally, zero.

Positive cash flow demonstrates high economic profitability and that the company has surplus cash. However, a positive treasury is not always a good sign (because resources are not attracted into efficient activities).

Negative cash flow reflects a financial imbalance, with the company having difficulty paying current debts to creditors.

Profitability can be defined as "the ability of an enterprise to make a profit from the use of inputs and capital, regardless of their source."

In particular, "profitability is a monetary surplus, i.e. the balance between total receipts and total expenditure. This notion of profitability is based solely on financial flows as the basis of the economic calculation"

Being considered a significant module in financial analysis "the profitability of an enterprise is the most commonly used concept and can generally be expressed as the rate of return, as the ratio of an income earned during a given period of time to the mass of capital invested during that period".

Profitability is a prerequisite for achieving economic and financial equilibrium, and becomes a tool for informing decisions on asset management and maintaining the firm in the competitive environment of the market economy.

Profitability ratios are ratios established by comparing indicators of results: gross operating surplus, operating result, gross result, net result, with indicators expressing the means used to obtain profit.

Ratios of return are calculated by relating an indicator of result to a form of valuation of the economic capital used by the firm to carry out the process of economic activity.

This gives rise to the notion of economic profitability, which expresses the efficiency of the use of a firm's assets in carrying out its business.

The economic rate of return is an indicator that focuses on the efficiency of the capital allocated to assets and measures "the performance of the total assets of the enterprise, based on an economic result and the totality of the means used".

In calculating the economic rate of return, the numerator may use the operating result or gross operating surplus and the denominator may use the total economic means (total assets) or part thereof. The economic rate of return is independent of the financial structure (debt ratio), the tax policy for the taxation of profits, and exceptional items

Financial profitability expresses the correlation between profit and capital as sources of financing the activity of the enterprise and reflects the degree of remuneration of the capital invested in an enterprise by the owners. The analysis of the rate of return becomes important by determining the influence of the factors acting in the management of capital and the achievement of profit in the operating activity of the enterprise.

Indicators expressing the results of the company's economic activity

Indicators that reflect a company's performance can be divided into three broad categories according to their scope:

- performance indicators expressing the volume of activity carried out, such as:

Mc (trading margin),
Qex (output for the year),
CA (turnover) and
VA (value added);

The trade margin has the meaning of value added, i.e. it expresses the firm's ability to produce effects for its own effort. It is the primary indicator of the performance of a business.

The trade margin is a performance indicator specific to distribution enterprises, but it can also be determined for the purely commercial part of manufacturing enterprises. It allows comparisons to be made between businesses by branch of activity and is also an important step in the calculation of the "variable cost margin", on the basis of which the "break-even point of the business" is determined.

Output for the year is the value indicator that measures the entire activity carried out by the enterprise during a financial year. The output for the year is made up of the goods and services produced by the enterprise, regardless of their destination: sale, storage or fixed assets, and is valued as an overall output for the financial year. Expressing the actual level of activity of the enterprise, this intermediate balance is determined by adding together production sold and production stored and fixed assets.

Turnover measures the commercial performance of firms, reflecting their competitive strength and market position. The absolute level of turnover gives us information about the size of the business conducted by a firm over a period of time.

Turnover represents the total revenue earned from a firm's business activity over a given period of time (usually one year).

Turnover is the fundamental indicator of the activity of any enterprise, and is at the top of the performance indicators in so far as it determines the size of the profit and rate of return.

Depending on the level of turnover it can be determined whether the enterprise is sufficiently

important, whether its results are significant in relation to those of the sector, and its analysis also allows a permanent reporting on the strategic position of the company.

Every company is interested in increasing turnover with a view to achieving as high a profit as possible or a moderate but certain profit in the future.

Conceptually turnover can be approached as total turnover, average turnover, marginal turnover.

Total turnover (Turnover) expresses the total volume of a firm's business valued at market prices, i.e. total receipts.

Average turnover (AVR) reflects the revenue realised on a product: $CA = CA/q$, where q is the physical volume of total sales.

Marginal turnover (MR) expresses the change in a firm's receipts when the quantity sold increases or decreases by one unit: $MR_m = \Delta MR / \Delta Q$

Value added reflects the added value (wealth) obtained through the productive and commercial activity of an enterprise. Value added is one of the most important indicators of a firm's economic and financial performance. Based on value added we believe that the true size of a firm's activity can be assessed.

Unlike turnover, which also includes the value of purchases of raw materials, materials and services, which are included in the turnover of supplier firms, value added only includes the equivalent of the activity of the enterprise in question.

As an analytical tool, value added makes it possible to assess the economic and financial performance of an enterprise: real economic power, the contribution of factors of production to the creation of wealth, the degree of economic integration, the contribution to GDP creation, etc..

- In this sense value added includes remuneration:
- labour through personnel costs;
- equity capital through dividends;
- technical capital, through depreciation;
- borrowed capital, through interest;
- the State, through taxes and duties.

Value added analysis at enterprise level involves:

- a) analysis of the dynamics
- b) analysis of structure
- c) analysis of influencing factors

The analysis of the dynamics of value added is assessed with the indicator growth rate of value added in year 1 compared to year 0.

The analysis of the structure of value added involves the analysis of the component elements, i.e. remuneration of labour, remuneration of equity capital, remuneration of the state, remuneration of creditors and remuneration of shareholders.

Analysis of the influencing factors, the influencing factors of value added are output for the year and intermediate consumption. In this respect, the influence of output on value added and the influence of intermediate consumption on value added are analysed

– profit-type performance indicators such as: R_{brut} E (gross operating result), RE, Rc (current result), REx (result for the year), REo (extraordinary result);

– performance indicators expressing financing potential: CAF (self-financing capacity), self-financing and cash flow.

Gross operating surplus is considered the first partial indicator of profitability, signifying the potential cash flow from a company's operating activity. This indicator best captures the ability of the operating activity to generate profit, as it is not affected by the main policies of the company: depreciation policy, financial policy and government tax policy.

It can thus be said that this result has three major destinations: return on invested capital (own or borrowed); return to the State through direct taxes (corporate income tax); maintenance of the economic-productive substance of the enterprise (self-financing).

Specific to this indicator, considered as cash flow from operating activities, is the fact that the result it shows is formed by relating monetary expenditure

(corresponding to actual payments) to monetary income (which is followed by receipts) and excludes those receipts and expenditure which are not relevant in monetary terms (income from provisions, depreciation and provisions).

The operating result is a more synthetic expression of the performance of the firm's operating activity, since it is obtained by deducting all operating expenses from all operating income. The operating result is not affected by the financial policy promoted by the company or by the fiscal policy of the State. On the other hand, this result may vary from one economic operator to another, depending on the depreciation and provisioning policy promoted by the company's management.

The operating result expresses the absolute size of the profitability of the operating activity and, compared with the result for the year, is of greater significance because, being independent of extraordinary items and income tax, it reflects the company's real effort to achieve results.

The current result shows the result of current operations carried out at company level, including, in addition to the result of operating operations, the result of financial operations.

The result for the year reflects the overall profitability of the company, representing what remains after deducting all expenses incurred during a financial year (including income tax expenses) from total income.

Self-financing capacity (SFF) is "the actual or potential monetary surplus arising from all management operations which remains available to the enterprise over the long term". This is a more complex indicator than net profit, since it involves correcting it for non-payable expenses (which do not involve a cash outflow) and non-receivable (non-cash) income. The indicator expresses the monetary value of the internal resources that a firm can allocate to finance its business maintenance and development needs.

Self-financing (AF) shows the surplus money available to the enterprise after all participants in the business have been remunerated beforehand (shareholders through dividends and employees through their wages). Self-financing gives a more accurate picture of the enterprise's ability to finance its development, calculated by subtracting from the value of the CAF the dividends distributed, i.e. the employees' profit-sharing.

Depending on its value in relation to CAF, we can identify three values of self-financing:

- $AF < CAF$ and $AF = \text{Depreciation}$, when all profit has been distributed;
- $AF < CAF$ partial self-financing, when part of the profit has been distributed and part is used for investment;

- $AF = CAF$, full self-financing, when all profit will be reinvested, the company does not pay dividends or equity

Cash flow is considered the newest expression of financial performance (Ganea, 2012) and is used in a complementary way to profitability ratios to help manage and measure firm performance. Its use in analysis eliminates one of the disadvantages attributed to profit - its historical nature. According to the same author, cash flows can be interpreted as a certain performance, whereas profit is

only a probable performance. Thus, cash flow is seen as a resource that the firm actually owns, whereas profit is a potential outcome.

In the most simplified approach, cash flow is the difference between cash inflows and cash outflows, at the level of a project, an investment, or often at the level of the whole firm. Two methods are used to determine the value of cash flow: the direct method and the indirect method.

Profitability ratios, profitability ratios and stock market return ratios are the most widely used indicators, both by management and shareholders, to measure company performance. Moreover, because they take into account all stages of the economic cycle (supply, production and marketing), profitability and profitability are considered to be among the most synthetic forms of expressing the efficiency of a company's economic and financial activity.

Although they are treated differently in the Romanian literature, profitability and profitability have the same basic meaning (profitability) - the ability of the company to generate profit

The profitability rate reflects the ability of a company to achieve a certain level of profit for a given volume of business. The following ratios are usually used to express profitability ratios: commercial profitability ratio (relates operating result/operating year/gross operating surplus to turnover), total revenue profitability ratio (relates result to total revenue) and consumed resources profitability ratio (calculates the ratio of result to total costs). All profitability ratios are calculated as percentage magnitudes.

The rate of return reflects the extent to which the capital at the company's disposal, i.e. the economic means held by the company, generates profit. The following ratios are usually used to express profitability: economic rate of return (reflects the percentage ratio between the economic result and the economic means used to obtain it) and financial rate of return (expresses the percentage ratio between the result and the financial resources available to the company).

Profitability can be defined as "the ability of an enterprise to make a profit from the use of factors of production and capital, irrespective of their source".

In other words, "profitability represents a monetary surplus, i.e. the balance between total receipts and total expenditure. This notion of profitability is based exclusively on financial flows as the basis of the economic calculation".

As it is considered a significant module in financial analysis, "the profitability of an enterprise is the most commonly used concept and can generally be expressed by the rate of return, as the ratio between an income earned over a given period of time and the amount of capital invested over that period".

Profitability is a prerequisite for achieving economic and financial equilibrium and becomes a tool for substantiating decisions concerning the management of assets and maintaining the firm in the competitive environment of the market economy.

Profitability ratios are ratios established by comparing indicators of results: gross operating surplus, operating result, gross result, net result, with indicators expressing the means used to obtain profit.

Ratios of return are calculated by relating an indicator of result to a form of valuation of the economic capital used by the firm to carry out the process of economic activity. This gives rise to the notion of economic profitability, which expresses the efficiency of the use of a firm's assets in carrying out its business.

The economic rate of return is an indicator that focuses on the efficiency of the capital allocated to assets and measures "the performance of the total assets of the enterprise, based on an economic result and the totality of the means used".

The results that can be used for profitability analysis are gross operating surplus, operating result, financial result, current result, extraordinary result, result before tax and interest and result for the year (before and after tax).

The financial resources taken into account for the analysis of financial rates of return and which are in the form of capital at the company's disposal are equity capital (for the financial return on equity), permanent capital (for the financial return on permanent capital) and invested capital (for the financial return on invested capital).

In the case of the analysis of economic rates of return, the economic means used by the company and used in the calculation are expressed as total assets (for the economic return on total assets), economic assets (for the economic return on economic assets) and operating assets (for the economic return on operating assets).

The distinction between profitability rates and rates of return can be seen not only from the way they are defined, but also from the way they are constructed: Profitability ratios are expressed as an effect/effect ratio, i.e. 'relates the various forms of profit expressing indicators to indicators expressing the activity carried out', whereas profitability ratios are expressed as an effect/effort ratio, i.e. 'relates the various forms of profit expressing indicators to indicators expressing the effort expended by the company in providing the conditions for carrying out the activity (total assets or capital)'.

Regardless of the form in which they are found, profitability ratios reflect the different forms of profit as a result of the combined effects of asset and liability management, while profitability ratios reflect how profit is associated with revenues (sales or total) and the consumption of these revenues.

Stock market yields, the subject of fundamental analysis, express the economic and financial performance of listed companies, responding to the interests of shareholders and investors in the financial market. The specific indicators of stock market yields are: earnings per share, market capitalisation, market capitalisation ratio, dividend per share, dividend capitalisation ratio.

One of the most commonly used stock market return indicators is the Tobin Q coefficient developed by Nobel laureate James Tobin in 1968. A low value (between 0 and 1) indicates that the cost of replacing the firm's assets is higher than the value of its shares. Conversely, a high Tobin Q (above 1) shows that the firm's shares are overvalued in the market.

Indicators expressing value creation

The new definitions of performance imply that a company is performing well when it delivers value to all its stakeholders. Both financial and non-financial indicators are used to capture value creation across the firm.

Well-known financial indicators are EVA (Economic Value Added), SVA (Shareholder Value Added), MVA (Market Value Added), CFROI (Cash Flow Return on Investment), CVA (Cash Value Added), plus indicators calculated using score-based methods, which include both financial and non-financial indicators, such as: Balanced Score Card; Intangible Assets Monitor; Skandia Navigator.

Economic value added is considered to be the most important indicator in this set, representing "the surplus value created by an enterprise from its operating activity after covering the cost of capital employed and taxes on profits". Invested capital includes capital employed (equity and long-term debt), to which the firm's short-term debt is added. Thus, the cost of invested capital can be seen as having two main components: the cost of equity capital and the cost of borrowed capital. We must also consider the market value of the invested capital, as this is the only way to accurately measure the surplus value created in the indebted firm.

ANNEXES

EXAMPLES OF ACCOUNTING INSTRUMENTS REGARDING BUSINESS MANAGEMENT DECISIONS

STUDY 1

Based on the data obtained from the annual financial statements for 2017 and 2018 provided by ABC, the following indicators and their dynamics were calculated:

Table 1. Dynamics of the Equity Assets

-lei-					
No. crt.	Specification		UM	The analysis period	
				2017	2018
1	FIXED ASSETS	Intangible assets	lei	4.963	3.222
			%	100	64,92
		Fixed assets tangible	lei	124.312.053	151.787.727
			%	100	122,1
		Immobilisations financial	lei	2.700	8.240
			%	100	305,19
		Fixed assets total	lei	124.319.716	151.799.189
			%	100	122,1
2	WORKING ASSETS	Stocks	lei	1.954.378	1.221.078
			%	100	62,48
		Receivables	lei	16.057.717	36.723.517
			%	100	228,7
		Cash and bank account	lei	1.551.059	1.806.828
			%	100	116,49
		Working assets total	lei	19.563.154	39.751.423
			%	100	203,2
3	PREPAID EXPENSES	Amounts to be taken back within one year	lei	61.784	107.344
			%	100	173,74
		Amounts to be taken back in more than one year	lei	0	0
			%	100	100
TOTAL ASSETS			lei	143.944.654	191.657.956
			%	100	133,13

Source: Financial statements and our own calculations

According to the data from the Financial Statements, the evolution of ABC's economic means for the period 2017-2018 has been calculated (Table 1). As a first conclusion, the upward trend of tangible fixed assets is observed as a result of the investments made by the company in fixed assets and buildings. The same pattern is also observed for the value of financial fixed assets, therefore the

company has receivables to be collected in a period longer than 1 year. Although there is a slight decrease in intangible assets, overall the firm's wealth is increasing year on year, which is a platform for financial prosperity. During the two financial years under review, the company has seen a slight decrease in inventories as a result of the optimization of production processes. The company's cash position shows a slight increase, contributing to the general trend of an increase in current assets, a large proportion of which is represented by amounts to be recovered in less than one year, for which the company must make efforts to cover its current needs.

As regards resources, obligations and liabilities, these have been analyzed in Table 2.

Table 2. Dynamics of Equity Liabilities

			-lei-		
No. crt.	Specification	UM	The analysis period		
			2017	2018	
1	CAPITAL EQUITY	Social capital	lei	117.551.720	117.551.720
			%	100	100
	Reported profit	lei	-2.454.432	-2.583.098	
		%	100	105,24	
	Reserve	lei	0	91.964	
		%	100	100	
	Result of the financial year	lei	-128.666	1.498.487	
		%	100	1164,63	
Total equity capital	lei	114.968.622	116.467.109		
	%	100	101,3		
2	TOTAL DEBTS	Debts amounts to be paid within a period of up to one year	lei	28.597.627	6.582.865
			%	100	23,02
	Debts amounts to be paid over a period of more than one year	lei	378.405	68.607.982	
		%	100	18130,83	
	Total debts	lei	28.976.032	75.190.847	
		%	100	259,49	
TOTAL LIABILITIES			lei	143.944.654	191.657.956
			%	100	133,13

An analysis of the balance sheet data shows that the level of resources at the company's disposal was unsatisfactory at the end of the first year under review, partly as a result of the company's investments in increasing production capacity. The level of net assets during the period under review shows an upward trend,

particularly at the end of 2018 when the positive return on investments made generated a year-end with a considerable increase in retained earnings. The other important component forming the equity liabilities, total liabilities, is on an upward slope, the effect of the company's investment policy. There is thus a decrease in short-term debt, which shows that the company is well able to pay its current debts, thus generating a climate of good relations with suppliers.

On the basis of the Profit and Loss accounts, the indicators of expenditure, income and financial result were analyzed (Table 3)

Analysis of the Profit and Loss Account

Table 3 Dynamics of the Profit and Loss Account

-lei-				
Nr. crt.	Specification	U. M.	2017	2018
1	Total expenditure	Lei	16.373.372	18.951.444
		%	100	115,75
2	Total income	Lei	16.291.145	20.790.717
		%	100	127,62
3	Profit/loss	Lei	-82.227	1.839.273
		%	100	2236,82

The consumption of human, material and financial resources is part of the total expenditure. The analysis of total expenditure reflects in value form the total consumption of factors of production, material, human and financial resources, which are used to produce and sell output. The structure and dynamics of these expenditures reflect the efficiency of the use of resources available to the enterprise. At the level of the analysis period, the company records an increase in total expenses, which in the first year failed to correlate with the level of total revenues, resulting in reported losses. Total revenue, which is formed by correlating production sold, services rendered, and financial income, records an increase at the level of 2018, exceeding the volume of total expenses, generating the end of the financial year with a positive result.

Based on the total turnovers from the trial balances and annual statements, expenditure data were taken (Table 4).

Table 4. Dynamics of total expenditure

-lei-				
Nr. crt.	Indicators	U. M.	2017	2018
1	Operating expenditure	Lei	14.976.888	18.534.864
		%	100	123,76
2	Financial expenditure	Lei	1.396.484	416.580
		%	100	29,83
3	TOTAL EXPENDITURE	Lei	16.373.372	18.951.444
		%	100	115,75

Source: profit and loss account and own calculations

Operating expenses are made up of the expenses necessary for the performance of the undertaking's activities, such as: expenditure on raw materials and consumables, other material expenses, expenditure on goods, expenditure on staff (wages and social security contributions), and value adjustments in respect of tangible and intangible fixed assets and expenditure on external services, as well as expenditure on taxes, duties and accrued charges (including taxes and duties incurred by the undertaking irrespective of the result for the financial year; such as tax on buildings, tax on means of transport, etc.).) from which trade discounts received are deducted. An analysis of the data in the Profit and Loss Account shows an increase in the level of operating expenses, which the company must monitor closely and which must be correlated with an increase in the level of income in order to maintain financial prosperity.

As for financial expenses, these result from the company's spending on financing decisions, investment decisions, exposure to foreign exchange fluctuations or provincial taxes. Following the analysis of the data in the Profit and Loss Account, the analyzed company recorded throughout the analysis period only financial expenses that fall under the category of Other financial expenses (the majority share being generated by account 665 Expenses from exchange rate differences - as the company also has suppliers that issue invoices in other currencies).

As can be seen, the very high share of operating expenses in total expenses indicates that the company is directing a large part of its expenses towards its own production activity, choosing not to rely on external sources of financing. Revenues have been taken both from the total turnover in the financial statements as at 31.12.2017 and 31.12.2018, as well as from the information data provided by the company under study (Table 5)

Table 5. Dynamics of total income

-lei-				
Nr. crt.	Indicators	U. M.	2017	2018
1	Operating income	Lei	15.639.673	20.489.757
		%	100	131,01
2	Financial income	Lei	651.472	300.960
		%	100	46,20
3	TOTAL INCOME	Lei	16.291.145	20.790.717
		%	100	127,62

The total revenue recorded is made up of revenue from operating activity and financial activity. The operating income includes income from production sold, income from operating subsidies, income from the sale of goods (which forms turnover), income from the production of tangible and intangible fixed assets and other operating income. In the case of the company analyzed, operating income is made up almost exclusively of income from the sale of production. As in the case of operating expenses, an increase can be observed in operating income, which facilitated the recording of a positive result for the year.

Financial income is earned by the company from activities related to financing decisions, investments, exposure to foreign exchange fluctuations or provisions made. Financial income comprises: income from participating interests, other fixed assets and non-current receivables, income from marketable securities, interest income, provisions, income from exchange rate differences and other financial income. In the case of the firm under review, the financial income obtained is mainly income from favourable exchange rate differences (account 765).

As regards the operating expenditure situation, the weighting of each item is shown in Table 6.

Table 6. Analysis of the structure of operating expenditure

-lei-				
No. crt.	Specification	U. M.	Period of analysis	
			2017	2018
1	Expenditure on raw materials and consumables	Lei	424.457	979.341
		% in total expenditure	2,59	5,17
2	Other material expenditure	Lei	95.214	137.458
		% in total expenditure	0,58	0,73
3	Other external expenditure (energy and water)	Lei	789.331	857.225
		% in total expenditure	4,82	4,52
4	Expenditure on goods	Lei	0	0
		% in total expenditure	0	0
5	Trade discounts received	Lei	582	26.093
		% in total expenditure	0,00	0,14
6	Staff expenditure	Lei	2.557.076	3.066.645
		% in total expenditure	15,62	16,18
7	Value adjustments on tangible and intangible assets	Lei	7.906.481	8.360.391
		% in total expenditure	48,29	44,11
8	Other operating expenditure	Lei	3.204.911	5.159.897
		% in total expenditure	19,57	27,23
9	TOTAL OPERATING EXPENDITURE	Lei	14.976.888	18.534.864
		% in total expenditure	91,47	97,80
10	TOTAL EXPENDITURE	Lei	16.373.372	18.951.444
		%	100	126,98

An analysis of operating expenses shows that value adjustments on tangible and intangible fixed assets account for a significant proportion of total expenses, averaging 46%. The volume of these expenses reflects the value of the company's investment in land, buildings and other fixed assets, as well as their

gradual depreciation (except for land, only land improvements are subject to depreciation). Another group of expenditure is increasing in value, although the share of total expenditure remains low, namely expenditure on raw materials and consumables, which doubled its volume during the two years under review, due to the increase in production.

Throughout the analysis period, the company is experiencing increases in operating expenses, which it will have to cover with operating income in order to achieve a positive operating result.

The evolution of operating revenues in 2017-2018 is presented in Table 7.

Table 7. Analysis of operating income dynamics

-lei-				
Nr. crt.	Indicators	UM	Period of analysis	
			2017	2018
1	Production sold	lei	15.633.560	20.375.356
		% in total income	95,96	98,00
2	Income from sale of goods	lei	0	0
		% in total income	0%	0%
3	Business turnover	lei	15.633.560	20.375.356
		%	100	130,33
4	Other operating income	lei	6.113	114.401
		% in total income	0,04	0,55
5	Operating revenue - TOTAL	lei	15.639.673	20.489.757
		% in total income	96,00	98,55
6	Income TOTAL	lei	16.291.145	20.790.717
		%	101	127,62

Source: Financial statements and own calculations

Operating income is made up of turnover (production sold and/or income from the sale of goods, income from operating subsidies) less income relating to the cost of production in progress, work in progress, with a final debit balance, plus income from the production of intangible and tangible fixed assets and other operating income.

From the analysis of the dynamics of the operating income, we can see that the overwhelming proportion comes from the production sold, also because the object of activity of the company - the cultivation of cereals (excluding rice), leguminous plants and oilseed producing plants, places it in the production sphere, thus the company does not record income from the sale of goods. The company did not receive any income from operating subsidies during the analysis period. Other operating income recorded by the company shows an upward trend, but has a low

share in total operating income, being made up of income from the stripping of fixed assets, . Throughout the analysis period, the company recorded an increase in operating income, as a result of efficient production management, managing to exceed the amount of operating expenses, generating a surplus from operating activity.

Analysis of the company's financial position

Financial equilibrium is the firm's ability to use its resources in such a way as to ensure its permanent solvency and profitability and its capacity to meet all its commitments while ensuring its development and maintaining a sustainable commercial relationship with its economic partners.

The financial position of an enterprise is the total assets and capital over which it exercises control. The analysis of the financial position is carried out on the basis of indicators determined using balance sheet information. Indicators are used for this purpose:

Net worth is a financial indicator that shows shareholders' wealth at a given point in time and is determined using the relationship: $NAA/NS = Total\ assets - Total\ liabilities$

This indicator expresses the book value of the wealth of the owners of the business, in other words, the shareholders/associates of the business.

If the company also records provisions or deferred income, the net position is determined by subtracting these from the total liabilities. Thus, the net position becomes equal to equity and expresses the value of the realisable assets at a given point in time in view of the liquidation of the business.

On the basis of the data presented in the company's accounting financial statements, the net position for the two-year period of analysis has been calculated and is shown in Table 8.

Table 8 Dynamics of the economic and financial potential indicator

-lei-				
Nr. crt.	Specification	UM	Period of analysis	
			2017	2018
1	Total assets	lei	143.944.654	191.657.956
		%	100%	133,15
2	Total debts	lei	28.976.032	75.190.847
		%	100%	259,49
3	Net situation	lei	114.968.622	116.467.109
		%	100%	101,30
4	Change in net position	lei	-128.666	1.498.487

Source: Financial statements and own calculations

The firm's net worth shows an increase over time due to the upward trend in the firm's total assets compared to total liabilities.

Throughout the period the net worth has increased, thus increasing shareholders' wealth and being a good proof of efficient financial management.

The indicator better reflects the value of realisable assets at a given point in time. This value is in fact the guarantee of the recovery of entitlements.

From a financial point of view, the balance sheet represents a balance between the resources attracted by the company (capital and liabilities) and the allocations made (assets). Working capital is a long-term financial balance indicator that checks the financing of assets with a maturity of more than one year from resources with a maturity of more than one year. In other words, it looks at the comparison of permanent resources (equity and long-term liabilities) with permanent allocations (fixed assets), according to the following calculation formula: ***FR = Permanent capital - Permanent allocations = Equity + Long-term liabilities - Net fixed assets.***

Working capital represents the part of the permanent capital remaining at the disposal of the company after the financing of fixed assets. It is therefore used by the company to finance short-term, highly liquid assets.

A high level of this indicator is undesirable, as it would imply long-term resources drawn in excess to finance current needs, and thus a mismanagement of financial management. Long-term resources cost the company money, with shareholders expecting additional remuneration in the form of dividends and creditors charging higher interest rates. It is preferable for working capital to be zero or as close to zero as possible. If the result is positive, the amount should not be large compared to the permanent capital. In the case of the company, the Anglo-Saxon version of the performance indicator of the working capital has been calculated on the basis of data taken from the balance sheets. Its analysis is shown in Table 9.

Table 9. Rolling Fund Analysis

-lei-				
Nr. crt.	Indicators	UM	Period of analysis	
			2017	2018
1	Permanent capital	lei	115.347.027	185.075.091
		%	100%	160,45
2	Fixed assets	lei	124.319.716	151.799.189
		%	100%	122,10
3	Bearing base	lei	-8.972.689	33.275.902
		%	100%	370,86

Source: Balance sheet and own calculations

During the period under analysis, the firm's inability to cover its permanent debts through permanent assets is noted, which leads to the recording of a negative working capital in the first year of analysis as a result of a negative ratio between the firm's other permanent resources and long-term debts.

In the second year of analysis, the firm's permanent capital exceeds its permanent resources, but does not reach the level of equity, generating a surplus that will be used to finance current assets.

There must be a balance between temporary needs and related resources, which is shown by the Working Capital Requirement indicator, which is determined as the difference between temporary needs excluding cash and temporary resources excluding bank loans. NFR management involves the management of suppliers, stocks, customers and treasury. Efficient NFR management will generate surplus liquidity, which reduces risks and increases profits.

The analysis of working capital requirements is shown in Table 10.

Table 10 Working Capital Requirement Analysis

-lei-				
Nr. crt.	Indicators	UM	Period of analysis	
			2017	2018
1	Working assets	lei	18.073.879	38.051.939
		%	100%	210,54
2	Current debts	lei	28.597.627	6.582.865
		%	100%	23,02
3	Necessary Working Capital Fund	lei	-10.523.748	31.469.074
		%	100%	299,03

Source: Financial statements and own calculations

At the end of the financial year of the first year of analysis, the company under review has a negative working capital requirement, which indicates that the company cannot cover its short-term debts by collecting receivables from cash on hand and by using existing stocks, but will have to resort to adding resources, either by using fixed assets or by adding funds. This was achieved the following year, when the financing of the short-term allocations was made from the working capital fund.

The liquidity-liability analysis continues with the comparative approach of the Working Capital Fund and the Working Capital Fund Requirement. The

difference between FR and NFR is represented by the net cash (NT), shown in Table 11.

Table 11 Analysis of Net Treasury

-lei-				
Nr. crt.	Indicators	UM	Period of analysis	
			2017	2018
1	Rulment Fund	lei	-8.972.689	33.275.902
		%	100%	370,86
2	Necessary Working Capital Fund	lei	-10.523.748	31.469.074
		%	100%	299,03
3	Net Treasury	lei	1.551.059	1.806.828
		%	100%	116,49

Source: Financial statements and own calculations

Treasury assets are the company's current liquid assets plus short-term investments (marketable securities). Treasury liabilities are basically current bank loans. A positive value of this indicator shows a surplus of liquid assets compared to immediate financial liabilities, which is desirable because it highlights the existence of the overall balance. In the two years in which the balance sheet data were analysed, positive values were recorded for net cash, indicating a state of equilibrium generated by the operating cycle management policy. At 2018 level, the Working Capital exceeds the Working Capital Requirement, which highlights a defensive policy adopted by the company's management, which involves achieving high turnover with high inventories and liquidity. This policy implies a prudent approach, rejecting the risk of current stock breakage, even if this aspect generates lower profitability. Therefore, for any increase in turnover, the unit's management is also concerned about the corresponding increase in stocks that ensure the continuity of the operating activity (current safety stocks). The financing of the financial needs of the operation is mainly provided by permanent resources (working capital) which have higher procurement costs but also sufficient coverage against the risk of credit renewal and interest rate increases.

Analysis of financial rates

The study of the enterprise's financial situation is deepened by the analysis of financial ratios, which looks at various aspects and has specific purposes. This analysis shows the extent to which the company can meet its payment obligations, how much it can finance itself through loans, how efficiently its assets are used and, last but not least, how efficient its management team is. In order to make the

analysis of financial ratios as effective as possible, it is recommended that the figures obtained by the firm in question be compared with those laid down in the regulations and those published by the National Statistical Commission as an average for the previous year for the same field of activity. This is necessary for a complete analysis of the firm in relation to the average of competing firms.

The indicators are grouped into 4 categories to meet the above objectives.

A. Financial rates of capacity to pay analysis

Most financial analysts believe that a manager's first concern is to see whether the company he or she is running can meet its payment obligations as they fall due in the near future. Two indicators are calculated for this:

- a) Current liquidity indicator
- b) Instant liquidity indicator

Current liquidity is one of a company's most important financial ratios and measures its ability to pay short-term debts using short-term assets on the balance sheet. It is calculated as the ratio of current assets to total short-term liabilities. The higher its value, the greater the company's ability to pay its current debts without drawing on long-term resources or new borrowing. The calculation of the liquidity ratios in the two years of analysis is shown in Table 12.

Table 12. Liquidity indicators

Indicators	Explication	Value	Year	
a) current liquidity ratio	Current assets/current liabilities	19.563.154/28.597.627	0,68	2017
		39.751.423/6.582.865	6,04	2018
b) Instant liquidity indicator	Current assets - stocks/current liabilities	17.608.776/28.597.627	0,62	2017
		38.530.345/6.582.685	5,85	2018

Source: Financial statements and own calculations

B. Financial rates of loan financing analysis

The extent to which loans are used for financing has multiple meanings. By using credit wisely, control of the business is maintained and the resources needed for the business are procured. Lenders want to know how much money the owners of the business are contributing to the business, so they know how secure the recovery of the credit they will grant is. The lenders' interest is therefore to recover the funds borrowed plus interest. The interest of the shareholders is that by using the loan funds they should make a sufficient profit to pay off their debts and remain with an adequate profit.

The following two rates are used to find out how much a business can be financed by loans:

- a) Debt ratio;
- b) Interest coverage ratio.

The debt ratio shows the share of debt in total assets; in other words, the debt ratio shows the share of borrowed loans in the total funds available to the firm. As a general rule, creditors prefer low debt ratios because the lower the debt ratio, the lower the risk of losses in the event of bankruptcy. Shareholders usually seek a higher rate because they want to grow their business and need to borrow to do so. However, too high a debt ratio usually leads to speculative actions by business owners. Since the funds they have invested are few and limited, the temptation to participate in some speculative actions is extremely high. If successful, speculation brings large gains to shareholders, but if unsuccessful, most of the loss goes to creditors.

The interest coverage ratio expresses the extent to which revenues can fall without causing financial problems for the firm (such as inability to pay its annual interest). The indicator is important because if the company can no longer meet its annual interest payment obligations, it will be taken to court by creditors and this is the first step towards bankruptcy. This indicator is determined by dividing the value of the firm's profits before interest and tax payments by the value of interest expenses. The risk indicators are given below.

Table 13 Leverage indicators

Indicators	Explication	Value		Year
a) the debt ratio indicator	Total debts/Total assets x 100	28.976.032/143.944.654 X 100	15,12	2017
		75.190.847/191.657.956 X 100	39,23	2018
b) the interest cover indicator	Profit before interest and income tax/interest expense	82.227/0	0	2017
		1.839.273 / 0	0	2018

Source: Balance sheet and own calculations

C. Financial ratios for analyzing the efficiency of asset utilization

The degree of efficiency with which the firm uses its assets should be a continuous concern of financial managers in order to ensure a certain balance between turnover and assets. It has almost been proven that high turnover is not the same as high profit. There are a number of assets whose excessive value can

paradoxically cause many problems for the company. For example, even if a company has money to receive from customers and in the balance sheet this is shown as an asset, if customers do not pay on time it can quickly lead to insolvency (no money to pay salaries, tax obligations, etc.). Also, the firm may have stocks recorded in the accounts at a certain value, but if they are old or depreciated, their real value is much lower.

The following indicators are used to determine the degree of efficiency of asset utilizations:

- a) Stock turnover rate;
- b) Average customer collection time;
- c) Utilisation rate of fixed assets;
- d) Turnover rate of fixed assets;
- e) Turnover rate of total assets..

The inventory turnover rate is calculated by dividing the turnover by the value of stocks. Controlling the value and size of stocks is one of the keys to success in business at the moment. Basically, a company cannot operate without stock, but at the same time too much stock can lead to a financial bottleneck by tying up the money with which it was bought. In calculating and interpreting stock turnover there are three problems which the financial manager should bear in mind:

- Turnover is expressed at market price, while stocks are taken into account at their book value (value at the date they were acquired);
- several methods can be used to value stocks (**FIFO** - *first in, first out, first in, first out*; **LIFO** - *last in, first out, last in, first out*) which can lead to different interpretations; WAC (weighted average cost). This determines the cost of each item, based on the weighted average of the costs of similar items in stock at the beginning of the period and items purchased or produced during the period. The final stock is assigned the calculated weighted average cost.
- In the calculation of the rates, annual sales are taken into account, while stocks are considered at a given value.

The average time taken to collect from customers indicates the number of days between the delivery of goods, execution of works, provision of services and the collection of the payment. In a general way, this indicator shows how many days a company receives the money for the products sold. This indicator has 2 stages in which it is determined: in the first stage, the annual turnover is divided by 365 days to determine the average daily sales; and in the second stage, the amount of bills receivable is divided by the average daily sales to find the average number of days in which money is received from customers.

The rate of utilization of fixed assets measures the efficiency with which the company uses the machinery and equipment at its disposal. It is calculated by dividing turnover by the net value of fixed assets (total value of assets less depreciation). The higher the value of the indicator, the more efficient the use of fixed assets, and the higher the value of the ratio, the more likely it is that the fixed assets are being used efficiently; there is cause for concern when the ratio approaches 1.

Table 14 Risk Indicators

Indicators	Explication		Value	Year
a) stock rotation speed	Turnover/stock value	15.633.560/1.954.378	8,00	2017
		20.375.356/1.221.078	16,69	2018
b) total customer throughput speed	Customers/Daily sales (=CA/365)	3.206.539/42.831,67	74,86	2017
		2.875.649/55.822,89	51,51	2018
c) speed of totalisation of supplier credits	Average balance suppliers/purchases of goods X 365	41.800/1.423,76	29,36	2017
		529.211/1.116.799 x 365	172,96	2018
d) speed of totalisation of fixed assets	Turnover/fixed assets	15.633.560/124.319.716	0,13	2017
		20.375.356/151.799.189	0,13	2018
e) total asset velocity	Turnover/total assets	15.633.560/143.944.654	0,11	2017
		20.375.356/191.657.956	0,11	2018

Source: Financial statements and own calculations

D. Financial rates of analysis of the effectiveness of the management team

Making a profit is the motivation of any business and the result of a set of strategic and tactical decisions by managers. Three indicators are used to measure how efficiently a business is run in terms of profitability:

- profit rate;
- return on investment;
- financial rate of return..

The profit rate reflects the profit earned per monetary unit of turnover and is calculated by dividing net profit (after tax) by turnover, the result being reported as a percentage. Obtaining as high a profit rate as possible should be an objective pursued by any business manager. The profit rate shows the net result of the combined effects of liquidity, asset management and debt management.

Return on investment measures the degree of return on all capital invested in the firm and is calculated as the percentage ratio of net profit to total assets.

The financial rate of return measures the degree of profitability of the investment made by shareholders. This rate is of most interest to the shareholders of a company, showing the true value of the investment made and is defined as the ratio of net profit to the value of equity.

The calculation of these indicators for 2018 is shown below in Table 15:

Table 15 Profitability Indicators

- at 2018 level			
a) return on capital employed	Net profit/Turnover x 100	$1.498.487/20.375.356 \times 100$	7,35
b) return on investment	Net profit/total assets x 100	$1.498.487/191.657.956 \times 100$	0,78
c) financial profitability	Net profit/equity x 100	$4.498.487/116.467.109 \times 100$	1,29

Source: Financial statements and own calculations






Global analysis of economic indicators

In order to establish an accurate diagnosis, the calculation of the indicators obtained at company level must be correlated with the average of the sector in which the company is active. Their analysis is given below:



Figure 1 Analysis of profitability indicators

Table 16 Profitability

Indicators	Evaluation	2018	Media sector
Net Profit Margin = $\frac{\text{Net profit}}{\text{Turnover}} \%$		7.35 %	9.41 %
Operating Profit Margin = $\frac{\text{Profit from operations}}{\text{Turnover}} \%$		9.59 %	11.68 %
Growth of Turnover = $\frac{CA\ 2018 - CA\ 2017}{CA\ 2017} \%$		30.33 %	9.83 %
Return on Assets = $\frac{\text{Net Profit}}{\text{AFixed assets}} \%$		0.99 %	8.96 %
Return on Capital = $\frac{\text{Net Profit}}{\text{Equity capital}} \%$		1.29%	14.90 %

Source: Financial statements and own calculations

Net profit margin is a financial profitability indicator that shows us in percentage terms how profitable a company's overall business is. It is a comparison between profit after tax and net sales and shows the profit remaining after all production and administration costs have been deducted from sales and income tax recognised. It is one of the best measures of a company's performance especially if combined with an assessment of how working capital is being used. It should also be noted that entities may deliberately keep this indicator low through a variety of expense recording strategies in order to pay lower corporation tax.

According to the result, the entity's situation is stable, as it falls within the 1%-15% range according to which stable firms fall, but the result recorded places it slightly below the level of industry competitors.

Operating margin shows how much of the company's turnover is operating profit. It is one of the most important financial ratios because it illustrates the company's ability to generate added value for shareholders.

A margin of 10%, for example, means that a product or service worth 100 lei sold resulted in an operating profit of 10 lei. Or, perhaps even more importantly, that the company managed to get 100 lei for 90 lei spent.

The operating result can be not only a profit but also a loss, in which case the operating margin is less relevant. As with most indicators, the values considered normal for operating margin depend on the sector of activity. In the case of the company under analysis, the operating margin is close to the average for the sector.

The company's objective, in terms of turnover, is to achieve continuous growth. The dynamics of turnover in 2018 show an increase of 33% compared to the previous year.

Return on assets is one of the main indicators of a company's profitability, and measures the efficiency of the use of assets in terms of the profit achieved.

While total asset turnover is how many lei of sales are obtained from one lei of assets, return on assets shows how many lei a lei invested in assets yields in the form of profit. Moreover, starting from its formula, $\text{net profit} / \text{total assets}$, the return on assets can be broken down, resulting in the formula **ROA = asset turnover * net margin (turnover / total assets) * (net profit / turnover)**, *where turnover is simplified and the original ROA formula itself results*).

The rate of return on assets calculated on the basis of balance sheet data in the case of the company is 0.99%, which means that for 1 leu of assets held the company generated, at the level of 2018, a profit of 1 penny, unlike the industry average which for the same value of an asset held obtained a profit of 9 money.

Return on equity is one of the most important indicators measuring a company's performance. The indicator is calculated as the ratio of net profit earned by the company to equity, basically expressing how well and efficiently shareholders have invested their money. The indicator allows to estimate the earnings per unit of capital invested in shares or the return to owners for the investments made in the company.

The value of the calculated return on equity indicator for the company is worryingly low, being below both the average interest rate, inflation and the average value recorded at industry level, which needs to be remedied in the future through a more efficient allocation of equity in order to increase the profit earned and meet shareholders' expectations.

Analysis of liquidity indicators

Table 17 Liquidity

Indicators	Evaluation	2017	2018	Sector average
<p>Current Rate</p> $= \frac{\text{Current assets}}{\text{Debt payment under 1 year}}$	✓	0.68	6.04	1.17
<p>Acid Test</p> $= \frac{\text{Current Assets} - \text{Stocks}}{\text{Debt payment under 1 year}}$	✓	0.62	5.85	0.74

Source: Financial statements and own calculations

Following the calculations made (Table 17), based on data from the Financial Statements, the company records a value of this indicator of 0.68 in 2017. According to OMF no.1802/2014, the recommended acceptable value is "around 2", although it is specified that the indicator provides coverage of current liabilities from current assets. In general, a current liquidity less than 0.8 is a negative signal. The optimal value for this indicator is around 1, but it can vary depending on the sector. Thus, there are sectors where optimal liquidity is 2 or even higher, but also sectors that perform very well at 1.5 or slightly below 1. In this case, the sector average was calculated and set as 1.17. In the first year of analysis, the case study company fails to come close to the sector average due to the high amount of short-term debt in relation to current assets. However, in 2018 there was a spectacular increase in the two indicators calculated, both in relation to the results recorded in the previous year and in relation to the sector average.

Analysis of solvency indicators

Table 18 SOLVENCY

Indicators	Evaluation	2018	Sector average
Total Indebtedness Ratio $= \frac{\text{Debts}}{\text{Total assets}} \%$	✓	39.23 %	62 %
Financial Indebtedness Ratio $= \frac{\text{Financial Debts}}{\text{Total assets}} \%$	✓	0.00 %	43 %
Debt Coverage Ratio $= \frac{\text{Profit from operations}}{\text{Debts Total}} \%$	✓	2.60 %	10 %
Degree of Interest Rate Coverage $= \frac{\text{Profit from operations}}{\text{Interest Expenses}}$	✓	100.00	7.16





Source: Financial statements and own calculations

Solvency and liquidity are terms that refer to the financial health of a company, but with some notable differences. Solvency refers to a company's ability to meet its long-term financial commitments. A solvent company is one that owns more than it owes; in other words, it has a positive net worth and manageable debt.

A company's financial health is also reflected by its debt ratio. This is determined as the ratio of total debt to total assets. It shows the extent to which the company's business is supported by borrowed money. In general, a gearing ratio of less than 60% is considered very good and reflects a long-term balance between internal and external sources of finance. At the end of the 2018 financial year, the company has a total gearing ratio of 39%, which is below the average for the sector and also below the recommended maximum, the optimum being 0.56. A leverage limit below 50% shows a high prudence in the company's risk exposure and a low appetite for credit-backed investment expansion. The low leverage also indicates the size of the reserves in borrowing, which is also reflected in the financial manager's decision not to borrow to finance the business.

Analysis of efficiency indicators

Table 19 Efficiency

Indicator	Evaluation	2018	Sector average
Customer collection period $= \frac{\text{claims}}{\text{turnover}} * 365 \text{ days}$		658 days	172 days
Suppliers payment period $= \frac{\text{suppliers}}{\text{operating expenses}} * 365 \text{ days}$		91 days	126 days
Stock rotation period $= \frac{\text{Stock}}{\text{material expenditure} + \text{goods} + \text{other mater}} * 365 \text{ days}$		24 days	114 days
Cash conversion cycle $= (\text{customer collections} + \text{stock rotation} + \text{payment to suppliers}) * \text{days}$		591 days	160 days

Source: Financial statements and own calculations

The average customer collection time, calculated in Table 2.19, is an economic and financial indicator that measures the "speed" of transformation of sales into receipts. It is useful to note that the sale of a product or service is recorded as revenue on the basis of the invoice issued to the customer. If the invoice is paid in part, then part of the revenue is recorded as receipts and the remainder as receivables (uncollected invoices). This indicator is calculated as the ratio of the amount of receivables to turnover which is indexed by the number of days in a calendar year, the result being expressed in days. The average collection period should be as short as possible so as not to affect the financial stability of the firm, i.e. the cash flow of the business. It is very important that sales growth targets do not also lead to an accelerated growth in receivables, which can cause bottlenecks in the business. The level of this indicator in the company is unsatisfactory in terms of the long period of time it takes for customers to collect their payment obligations, which should be a matter for the financial manager in order to avoid a situation that could lead to a lack of liquidity.

The turnover of debts to suppliers shows how many times the company pays its debts to suppliers during a year. It is hard to say that there is an optimal value for the indicator.

Depending on the specifics of each individual company, the turnover of debts to suppliers and especially its variation over time can help to draw conclusions and remedy any problems. For example, if the value of the indicator decreases over a period it means that the firm is taking longer to make payments to suppliers. This may mean that the company is no longer able to maintain a good payment rhythm to suppliers because of a worse business performance, but it may also mean that management has been able to negotiate better payment terms with suppliers, and this will help increase turnover and profit.

We must therefore also look at the company's situation and the events it is going through or has gone through in order to draw a relevant conclusion from the turnover of debts to suppliers. Calculation formula for the turnover of debts to suppliers: $(\text{Expenditure on raw materials and materials} + \text{Expenditure on goods} + \text{Other operating expenditure})^* / \text{Debts to suppliers}$.

Inventory turnover shows how many times the company's stocks are sold and replaced during a year, thus measuring how efficiently they are used. Obviously, a higher value means higher efficiency and a lower value means lower efficiency.

Depending on the company's sector of activity and its specific features, especially the higher or lower stocks it works with, the indicator can reach higher or lower values. In services, for example, its value will be maximum, because stocks are either non-existent or very low. In such cases, however, the relevance of this indicator is reduced. This is also the case for the company under analysis, as it provides seed processing services, both the volume of stocks and the value of the turnover indicator are low.

The number of days it takes for a company to recover the money it has spent in the operational process. It is calculated according to the formula "time to keep stocks" + "time to recover debts - time to pay suppliers". The explanation is as follows: raw material stocks are held for a period (stock holding period) until they are transformed into finished products, then another period (payables recovery period) until the finished products, once sold, generate a cash inflow. The point at which cash leaves the company is not when the raw materials are first held, but only after some time (the period of payment to suppliers). The point at which the cash outflow for the payment of raw materials is recovered is at the end of the debt recovery process. The difference between the two moments is the cash conversion cycle. This is a theoretical situation, in reality things are more complex, but the indicator gives a fairly accurate overall picture of how the company's business is going. Obviously, every company aims for a cash conversion cycle that is as short as possible, the ideal being that money is paid to suppliers on the same day that customers pay their debts (CCC=0). A lower conversion cycle results in less need

to finance current expenses through bank loans, hence lower interest costs and greater business stability.

Analysis of the enterprise's financial performance

The basis for financial decisions in order to optimize the creation and use of resources requires that the financial analysis approach is directed not only towards ways of achieving financial equilibrium, but also towards tracking the stages of money accumulation. In order to establish the financial performance of the enterprise, this is carried out on the basis of the profit and loss account. The profit and loss account centralizes the result of economic and financial inflows, outflows and outflows during the period under review. This type of financial analysis has two major components: interim management balances and self-financing capacity, which will be analyzed below.

Analysis of interim balances

A more accurate and relevant assessment of the company's financial situation requires the use of performance measurement tools that are likely to reflect the economic and financial reality of the activity carried out in a more meaningful way than that provided by the usual accounting indicators. The structure of the profit and loss account according to the three types of activity makes it possible to draw up balances of potential cash accruals intended to fulfil a certain function of remunerating the factors of production and financing future activity, known as interim management balances (IMB). Interim management balances represent the successive stages in the formation of the final result. The indicators are constructed in a cascade, starting with the most comprehensive (production for the year + trade margin) and ending with the most synthetic (net result for the year). Interim management balances take the information from the profit and loss account. The correspondence between the interim management balances, the financial statements (profit and loss account) and the accounts in the company's financial accounts is shown in Table 20.

Table 20 Trade margin

-lei-			
Nr. Crt.	Interim management balances	Financial exercise	
		2017	2018
1	Sales of goods (rd. 03 din CPP ¹)	0	0
2	Cheltuieli privind mărfurile (rd. 20 din CPP*)	0	0
3	Trade Margin (1-2)	0	0
Production of the exercise			-lei-
Nr.Crt.	Interim management balances	Financial exercise	
		2017	2018
1	Production sold (rd. 02 din CPP*)	15.633.560	20.375.356
2	Production in stock (rd. 07 din CPP*)	0	0
3	Capitalised production (rd. 09 din CPP*)	0	0
4	Production of the exercise (1+2+3)	15.633.560	20.375.356
Value added			-lei-
Nr.Crt.	Interim management balances	Financial exercise	
		2017	2018
1	Trade margin	0	0
2	Production of the exercise	15.633.560	20.375.356
3	Intermediate consumers (rd. 17+18+19+32 din CPP*)	4.065.690	6.896.470
4	Value added (1+2-3)	11.567.870	13.478.886

Source: Financial statements and own calculations

Analysis of the trade margin

The first indicator provided by the interim management balances table, Table 20, is the trade margin. This, together with the output for the year, is more an expression of the overall flow of activity than a true indicator of results. **The trade margin** (trade surplus) relates exclusively to commercial enterprises or only to the commercial activity of enterprises with a mixed activity (industrial and commercial). The excess of sales of goods over their purchase cost is the trade margin. The purchase cost of goods sold includes the purchase price (excluding VAT) plus incidental purchase costs and adjusted for changes in stocks of goods. In the situation encountered by the company, it should be noted that the production sold is made up exclusively of the consideration for services rendered, 100% of

¹* Profit and Loss Account

which is turnover, since the company does not earn any income from the sale of goods, interest or operating subsidies.

Analysis of exercise output

Production for the year, being the central concept in the calculation of interim management balances, together with the trading margin, deserves to be distinguished from the turnover indicator. In mixed enterprises, turnover shows sales of goods and output sold, whereas in industrial enterprises it reflects only output sold. By ignoring certain key aspects of the enterprise's activity, such as the time lag between manufacturing and invoicing, incurring income related to the cost of stocks of products, as well as fixed production, which can sometimes be significant, turnover can give a distorted picture of the enterprise's activity. On the contrary, the output for the year gives a more accurate picture of the undertaking's real activity during the management period.

In the case of the company analysed, an interesting aspect is noted: in the formation of the output indicator for the financial year, the only contribution is given by the output sold, which is made up of the value of the services provided, i.e. the income obtained by the company from the provision of processing services for maize, rapeseed, sunflower and soya beans, which is on an upward trend, an aspect that highlights the company's efforts to increase the volume of sales and justifies the investment decision.

Analysis of value added

Value added (Va), (the first intermediate balance of management), expresses the increase in value resulting from the use of factors of production, in particular labour and capital, over and above the value of goods and services provided by third parties in the enterprise's current activity. Value added is calculated on the basis of the output for the year plus the trade margin less the consumption of goods and services provided by third parties for this output.

Value added is not shown in the profit and loss account, but it contains the elements needed to determine the value added, in particular to determine consumption from third parties. This consumption comprises two main categories: supplies consumed (purchases of raw materials, other supplies + changes in stocks + non-stock purchases) and other external purchases consumed (works and services performed by third parties).

Analyzing the dynamics of the indicators forming the added value, in the case of the company, we observe the direction of growth of intermediate

consumption, which, although increasing in value in 2018 compared to the previous year, does so in a controlled context, as this growth is also correlated with an increase in the volume of sales.

Analysis of gross operating surplus, gross profit and net profit

In order to form as comprehensive an overview as possible of the state of the undertaking under review, the analysis of the interim management balances continues with the calculation of the gross operating surplus, gross profit and net profit, the results of which are shown in Table 21.

Gross operating surplus (GOS) or, where appropriate, Gross operating deficit (GOD), is the information obtained by the difference between value added (+ operating subsidies) on the one hand, and taxes, duties and personnel costs on the other.

The gross operating surplus expresses the gross accumulation from operating activity (operations strictly related to industrial production, commercial activity or the provision of services), the main resource of the enterprise, with a decisive influence on economic profitability and the potential self-financing capacity of investments (from depreciation, adjustments, profit).

Gross operating surplus is a measure of the economic performance of the enterprise. From this point of view, enterprises engaged in manufacturing and service activities achieve a significant gross operating surplus.

This is also the case for the company, which records positive values, and which is on an upward trend during the 2 years of analysis, of the indicator of operating activity, and which reflects the efficient extent to which the factors of production were used, the efficient manner in which the expenses with other taxes and duties were reduced, in 2018 compared to the previous year, as well as the lack of subsidies in the operating activity but also the volume of personnel expenses, which, although recording an increase, in 2018 compared to the previous year, are carried out against the background of an increase in the number of employees working within the framework of the enterprise; whereas at the end of 2017 the company had 11 employees, at the end of 2018 the number of employees was 25.

Table 21 Gross operating surplus, gross profit and net profit

No. crt.	Interim management balances	-lei-	
		Financial exercise	
		2017	2018
1	Gross value added	11.567.870	13.478.886
2	Operating grants (rd.12 din CPP*)	0	0
3	Expenditure on other taxes, duties and similar charges (rd.33 din CPP*)	441.536	172.715
4	Staff expenditure (rd.22 din CPP*)	2.557.076	3.066.645
5	Gross operating surplus (1+2-3-4)	8.569.258	10.239.526
6	Other operating income (rd. 13 din CPP*)	6.113	114.401
7	Income from value adjustments on tangible and intangible assets (rd.27 din CPP*)	0	0
8	Income from value adjustments on current assets (rd.30 din CPP*)	0	0
9	Income from provision adjustments (rd.41 din CPP*)	0	0
10	Other operating expenses (compensation expenses, donations and assets disposed of) (rd. 37 din CPP*)	6.687	64.736
11	Expenditure on value adjustments in respect of tangible and intangible assets (rd.26 din CPP*)	7.906.481	8.360.391
12	Value adjustment expenses on current assets (rd. 29 din CPP*)	0	0
13	Expenditure on provision adjustments (rd. 40 din CPP*)	0	0
14	Operating result (5+6+7+8+9-10-11-12-13)	662.203	1.928.800
15	Financial income (rd.52 din CPP*)	651.472	300.960
16	Financial expenditure (rd.59 din CPP*)	1.396.484	416.580
17	The financial result (15-16)	-745.012	-115.620
18	Gross result of the year (14+17)	-82.809	1.813.180
19	Corporate income tax (rd.66 din CPP*)	46.439	340.786
20	Net result of the year (18-19)	-129.248	1.472.394

Source: Financial statements and own calculations

Operating result (Rex), is another measure that relates to the operating and current activity of the enterprise. By deducting depreciation charges and adjustments from gross operating surplus, it becomes net operating result. The operating result expresses the absolute size of the profitability of the operating

activity, obtained by deducting all expenses (payable and calculated) from the operating income (receivable and calculated).

The size of this indicator is strongly influenced by the high amount of depreciation made by the company in the two years under review. The high amount of monthly and, ultimately, annual depreciation is determined by the amount of investment made by the company in the fixed assets and machinery needed to carry out the seed reception, grading and treatment process.

The financial result (FR) represents the result of operations generating financial income and operations giving rise to financial expenses. It is obtained by the difference between financial income and financial expenses. This balance allows, in the absence of disturbing elements which would falsify the realism of some calculations, the comparison of performance between undertakings, or of performance from one financial year to another. A comparison in space and time.

The analysis of the data provided by the company shows that the financial charges cannot be covered by financial income, which leads to negative financial results in both years of analysis.

The gross result for the year represents the "Income" derived from operating activities and made available to equity and debt contributors (shareholders, creditors). This result is therefore used to compare the performance of enterprises with different financial policies. It is obtained by adding the operating result to the financial result and is the result to be submitted to the general meeting of shareholders or associates, as the case may be, for a decision on distribution. Since in 2017 the financial result had a negative value that was not neutralised by the value of the operating result, the gross result for the year, recorded by the company, was negative; unlike the following year when the value of the operating result absorbed the negative result of the financial result, generating a positive value of the gross result for the year, available to shareholders and subject to taxation.

The net result of the exercise appears in a double hypothesis:

- as a relative indicator of the effectiveness of the company's industrial and/or commercial activity.
- as a measure of the flow of additional resources created by the enterprise (profit) or destroyed during the year (loss).

The net result for the year expresses the absolute size of the financial return, with which the shareholders will be remunerated for the equity subscribed. This net profit must be backed up by the existence of real monetary resources, otherwise it remains only a potential source of financing. The net result is to be distributed in the form of dividends and/or reinvested in the company. The

undistributed net profit is a source of own financing or a self-financing element generated by the enterprise's own activities.

Analysis of accumulation margins

In order to build up accumulation margins, a structural distribution of expenditure is necessary. In order to achieve this, the company's expenditure must be divided into variable and fixed. It should be noted that to determine the level of variable expenses, those expenses directly proportional to the volume of sales will be identified, and for the calculation of the level of fixed expenses - expenses not related to the volume of sales.

Often the division is difficult and varies from business to business. The division we made for this example considered a company in the industrial sector, where external expenditure on water and electricity is dependent on production, and the staff is entirely directly productive. These are shown in Table 22:

Table 22 Variable Expenditure

Nr. crt.	Variable Expenditure	Financial exercise -lei-	
		2017	2018
1	Expenditure on raw materials and consumables (ct.601 + 602)	424.457	979.341
2	Other material expenditure (ct. 603 + 604 + 606 + 608)	95.214	137.458
3	Other external expenditure (cu energie și apă) (ct.605)	789.331	857.225
4	Expenditure on goods (ct.607)	0	0
5	Staff expenditure (rd. 22 din Cpp*)	2.557.076	3.066.645
6	Expenditure on external benefits (ct. 611 + 612 + 613 + 614 + 615 + 621 + 622 + 623 + 624 + 625 + 626 + 627 + 628)	2.756.688	4.922.446
Total		6.622.766	9.963.115
Nr. crt.	Fixed Expenditure	Financial exercise -lei-	
		2017	2018
1	Expenditure on other taxes, duties and similar charges; expenditure on transfers and contributions payable under special legal acts (ct. 635 + 6586)	441.536	172.715
2	Other expenditure (ct. 651 + 6581 + 6582 + 6583 + 6584 + 6588)	6.687	64.736
3	Other financial expenditure (ct.663 + 664 + 665 + 667 + 668)	1.396.484	416.580
4	Value adjustments in respect of tangible and intangible fixed assets (Cpp. rd. 25*)	7.906.481	8.360.391
5	Provision adjustments (rd.39 din Cpp*)	0	0
6	Interest-related expenditure (ct.666)	0	0
Total		9.751.188	9.014.422

Finally, the accumulation margins obtained are shown in Table 23:

Table 23 Accumulation margins

		-lei-	
No .	Accumulation margins	Financial exercise	
		2017	2018
1	CA	15.633.5 60	20.375.3 56
2	CV (Production-related expenditure)	6.622.76 6	9.963.11 5
3	MVE = CA – CV	9.010.79 4	10.412.2 41
4	EBITDA = MCV + Any other operating income + Financial income + Provision reversal income - Fixed charges (excluding depreciation, net provisions and interest)	7.823.69 2	10.173.5 71
5	EBIT = EBITDA - Depreciation and net provisions (adjustments)	-82.809	1.813.18 0
6	EBT = EBIT - Interest-related expenditure	-82.809	1.813.18 0
7	RN = EBT - Corporate income tax	-129.248	1.472.39 4
8	EBIT - Corporate income tax = RN + Interest rates	-129.248	1.472.39 4

Source: Financial statements and own calculations

Note that in the conception of the accumulation margins described above, income is represented by turnover, and any other income encountered at the enterprise level is negligible compared to it. The margins do not have a direct correspondence in the profit and loss account according to Romanian legislation. Thus, in order to make an adjustment, we have included in profit before interest, tax, depreciation and amortisation income that does not represent turnover.

Margin on variable expenditure (MVE)

Represents the surplus from operating activity taking into account only variable costs. Determining it requires a distinction to be made between variable costs (directly proportional to sales volume) and fixed costs (unrelated to sales volume), which can be difficult and even arbitrary at times. MVE is calculated using the relationship: $MVE = CA - CV$. The calculations, based on the annual financial statements, show an upward trend in variable costs within the company, but this does not result in a low margin on variable costs, as the level of turnover is

also on an upward trend over the two-year period of analysis, thus covering the increase in variable costs.

Earnings before interest, taxes, depreciation and amortization (*EBITDA – earnings before interest, taxes, depreciation and amortization*)

It expresses the potential for self-financing of investments, for paying obligations to the state budget and for remunerating equity investors. It is one of the most important margins and has the advantage of not being influenced by investment policy (depreciation), financing policy (indebtedness of the company) or tax policy (taxation of profits). EBITDA is approximately equal to EBITDA in the statement of interim management balances and is determined with the formula: $EBITDA = MVE + \text{Any other operating income} + \text{Financial income} + \text{Income from reversal of provisions} - \text{Fixed expenses (excluding depreciation, net provisions and interest)}$. The value of this indicator is in line with the upward growth trend and is directly correlated with the evolution of the company's sales volume over the two years under review.

Profit before interest and tax (*EBIT – earnings before interest and taxes*)

It is often assimilated to operating profit, being a margin that shows the financial surplus without taking into account the financing policy (interest expenses), and is calculated as such: $EBIT = EBITDA - \text{Depreciation, amortisation and net provisions (adjustments)}$. This indicator shows negative values in 2017 in the company, due to the high amount at the level of depreciation of assets, which could not be covered by the income generated by operating activities. At the level of 2018, the situation improves, the operating result generates a surplus that assimilates the value of depreciation and generates a positive value of profit to be subject to taxation.

Profit before tax (*EBT – earnings before taxes*)

It is the result of the current activity of the enterprise and is determined by the formula: $EBT = EBIT - \text{Interest expense}$. In practice, within the company, this indicator is identical to earnings before interest and tax (EBIT) as a result of the management decision not to borrow; a situation valid for both years of analysis.

Net profit or net result (RN)

Represents the return to shareholders for the capital invested. If they make a profit, they may decide to distribute it in the form of dividends or reinvest it in the company as a source of self-financing growth. NR is expressed as follows: $NR = EBT - \text{Income tax}$. The difference between the net result and EBIT represents the amount of corporate income tax incurred by the company, which in the case of the company recorded values of 46,439 lei in 2017 and 340,786 lei in 2018.

The operating performance of the economic assets of the enterprise (equity and long-term liabilities) is measured by the potential return to investors

(shareholders - with profit, creditors - with interest) using the following margin: $EBIT - \text{Income tax} = NR + \text{Interest}$. The margin expresses the result of exploiting the economic asset, but also the beneficial effects of debt (tax savings generated by the deductibility of interest from taxable profits). Consequently, it does not only allow comparisons to be made between companies in terms of their technical and economic performance, but also in terms of the total gains obtained by long-term investors in the business. As the company under analysis did not incur any interest expenses during the 2 years of analysis, the value of this indicator is similar to the value of the net result indicator.

Analysis of self-financing capacity

Self-financing capacity (SFF) is a balance which is the difference between the inflows and outflows generated by current operations and shows the own resources remaining available to finance various needs: the result for the year after taxation and expenditure which did not involve payments (non-cash expenditure). The indicator therefore reflects resources for financing current and investment activities and for remunerating own capital (through dividends distributed to shareholders).

There are two methods of determining self-financing capacity: the deductive and the additive method.

The deductive method

It starts from the gross operating surplus: $EBITDA = EBITDA + \text{Other operating income} - \text{Other operating expenses (compensation expenses, donations and divested assets)} + \text{Financial income} - \text{Financial expenses} - \text{Income tax}$.

The additive method

It considers self-financing capacity seen as the difference between monetary income (receivable) and monetary expenditure (payable). Thus, the CAE is the monetary expression of accounting profit. To calculate it effectively, one can use the additive method, which corrects the net result by eliminating non-monetary items: $CAF = NR + \text{Non-monetary expenses} - \text{Non-monetary income} = NR + \text{Value adjustments on tangible and intangible assets} + \text{Value adjustments on current assets} + \text{Provision adjustments}$.

- a) In view of the profit and loss account of the company I propose to determine the self-financing capacity by the following methods:
- b) deductive;
- c) Additive.
- d) Self-financing capacity by the deductive method (Table 24):

Table 24 CAF (The deductive method)

-lei-			
Nr.crt.	CAF (The deductive method)	Financial exercise	
		2017	2018
1	EBE	8.569.258	10.239.526
2	Other operating income (rd.13 din Cpp)	6.113	114.401
3	Other operating expenses (compensation expenses, donations and assets disposed of) (rd.37 din Cpp)	6.687	64.736
4	Financial income (rd. 52 din Cpp)	651.472	300.960
5	Financial expenditure (rd. 59 din Cpp)	1.396.484	416.580
6	Corporate income tax (rd. 66 din Cpp)	46.439	340.786
7	CAF (1 + 2 - 3 + 4 - 5 - 6)	7.777.233	9.832.785

Source: Financial statements and own calculations

e) Additive self-financing capacity (Table 25):

Table 25 CAF (The additive method)

-lei-			
Nr.crt.	CAF (The additive method)	Financial exercise	
		2017	2018
1	RN	-129.248	1.472.394
2	Non-monetary expenditure (rd.26 +29 + 40 din Cpp)	7.906.481	8.360.391
3	Non-monetary income (rd. 27+ 30 + 41 din Cpp)	0	0
7	CAF (1 + 2 - 3)	7.777.233	9.832.785

Source: Financial statements and own calculations

As can be seen, both methods of determining the company's self-financing capacity in this case produce the same results, i.e. they illustrate the resources for financing current and investment activities and for remunerating equity (through dividends distributed to shareholders). At the end of the two exercises analysed, it is clear that efficient management is reflected in the constantly increasing value of the indicator showing self-financing capacity, and that the financial management's decision to finance the current activity from its own resources, without having to borrow, is justified.

Break-even analysis

The break-even point is that critical point at which the volume of sales covers the firm's fixed and variable costs, so that it makes neither a profit nor a loss. In other words, it is the point at which the firm starts to make a profit. The

break-even point is one of the most important analyses that a financial manager must make both when starting a new business and on an ongoing basis thereafter.

The simplest relationship for calculating the break-even point is expressed as follows: Turnover = Total expenses. At this point, the business result is zero. Dividing total costs into variable and fixed gives the following relationship: $Turnover - (Fixed\ expenses + Variable\ expenses) = 0$ or $Turnover = Sales\ price \times Quantity\ of\ products$.

In a business, **fixed costs** are those expenses that remain unchanged regardless of the volume of sales or business activity recorded. In other words, regardless of whether or not the business is producing, these costs remain unchanged. **Variable costs** are those that change in line with the volume of business activity - the higher the sales, the higher the variable costs.

Having said that, in the break-even analysis the minimum turnover that covers the total costs of the company or the change in price and quantity to reach this minimum turnover must be identified. The sales price analysis is one of the important elements of the break-even analysis. A change in it causes the break-even point in the firm to change. Thus, an increase in the selling price leads to higher receipts and the break-even point (the point at which receipts will equal costs) will be lower. On the other hand, the selling price cannot be easily changed, as it is dependent on market demand and supply for identical or substitute products or services..

The break-even point can be determined as follows:

$$v = \frac{CV}{CA}$$

where: v - share of variable costs in turnover.

In the case of the company the break-even point is as follows:

$$V_{2017} = \frac{6.622.766}{15.633.560} = \mathbf{0,42} \qquad V_{2018} = \frac{9.963.115}{20.375.356} = \mathbf{0,49}$$

where:

$$CA_{prag} = CV + CF$$

CA_{prag} – minimum turnover covering total costs (break-even point).

$$CA_{prag} = v \times CA + CF$$

$$(1 - v) \times CA_{prag} = CF$$

$$CA_{prag} = \frac{CF}{1 - v}$$

- $CA_{prag\ 2017} = \frac{9.751.188}{1-0,42} = \mathbf{16.812.393}$

- $CA_{prag\ 2018} = \frac{9.014.442}{1-0,49} = 17.675.376$

Analyzing the values obtained from the calculation of the break-even point we can see that in 2017 the break-even point of the turnover was not reached, as a result of this fact the company recorded losses unlike the following year when the break-even point was reached and exceeded generating the end of the year in the profit sphere.

The analysis of the financial position carried out on the business model of the. was a pertinent study of economic dynamics, based on figures and indicators that measure the economic strength of the company under analysis and highlights the strengths but also the things that need to be improved in the future.

The analysis of the financial position involved a broader and more complex analysis of the specific financial-accounting indicators, highlighting and calculating the liquidity, solvency, financial balance, working capital and working capital requirements ratios, the positive values of these indicators, assuming a long-term financial balance, the over-unified profitability, solvency and positive net cash ratios, gave a telling picture of the company's increased degree of economic and financial independence.

Its strengths were highlighted, consisting in the high degree of integration and specialization of activities, the reinvestment of profits which gives certainty of certain sources of financing for modernization and upgrading objectives, but also the points that need to be improved, the weaknesses.

The top management of the company must take into account in the future both the maintenance and improvement of the positive aspects, but must act by measures to eliminate the negative, weak points of the company, also to prevent the effects of threats, risks affecting the company's activity.

The proposed measures included:

- discovering new methods of processing processed seeds and targeting other areas in search of and finding commercial partners;
- reducing costs in all business segments;
- continued focus on strict cost management and organisational optimisation;
- developing multiple economic forecasts based on the most complex future scenarios;
- more efficient use of processing capacities;
- adapting to European environmental policy requirements;
- implementing high safety, security and environmental standards;

- increasing the availability in banks and placing it as advantageously as possible so that the company can pay its obligations in the shortest possible time, in accordance with the contractual clauses;
- selling or scrapping fixed assets that do not bring in a profit but generate maintenance costs;
- encouraging, supporting and stimulating the initiatives of competent persons;
- increasing performance by specialising employees;
- maintaining and developing the staff training and development programme;
- exchanges of experience with Remington Seeds LLC. employees in other countries;

Despite the unfavourable conditions of Romanian agriculture, through its staff, through the management adopted, it manages to maintain and consolidate its position on the seed processor market. Most of the indicators calculated and analysed within the project show and demonstrate that the company has a solid economic position, and in the case of the indicators that show decreasing trends, it has reviewed its development options and changed its future strategies in order to maintain its economic and financial balance.

Accurate reflection of economic and financial reality and its social, human and institutional consequences are the defining attributes of accounting, for the perfection of which the most redoubtable specialists in the "science of accounts" are striving and working today. Concerned with standards, convergence and the accounting reflection of reality, accounting professionals are in fact concerned with the economy, institutions and people. This is perhaps the best part of the accounting profession. It is one of the reasons why the European Union has taken the opportunity to recognize the accounting profession at European level and it is also one of the reasons why I have chosen and enjoy this profession.

STUDY 2

The case study was made at the company Bucium SA from Iasi and the data from the annual financial statements were used, during 2019-2020. The data used to perform the analysis of the dynamics of the financial rate of return belong to an economic operator with a productive activity profile. These are presented in the following table. The system of accounting indicators used in the calculation and analysis of the performance pyramid *in lei* is present in table 1.

Table 1 Analysis of the performance pyramid

Nr. crt.	Indicators	2019	2020
1	Fixed assets	26.380.188	22.581.998
	• Intangible assets	0	0
	• Property, plant and equipment	26.378.868	22.576.564
	• Financial assets	1320	5.434
27	Current assets	9.417.632	9.711.252
	• Inventories	6.440.601	6.609.566
	• Receivables	2.742.363	2.813.648
	• Short-term investments	0	0
	• House and bank accounts	234.668	288.038
3	Expenses registered in advance	2.982	38.672
4	TOTAL ASSETS = TOTAL LIABILITIES	35.800.802	32.331.922
5	Total debts	8.496.325	10.795.078
6	Own capital	25.044.547	15.956.590
7	Advance income	2.259.930	5.580.254
8	Fiscal value	13.067.583	13.815.331
9	Net profit (Net result)	1.031.698	859.222
10	Tax	189.867	82.240
11	Gross profit (Gross result)	1.221.565	941.462
12	Interest expenses related to contracted loans	233.095	218.624
13	Economic result (Gross profit + Interest expenses)	1.454.660	1.160.086

The system of derived indicators necessary for the elaboration and analysis of the performance pyramid is presented in the table below. The system of derivative indicators calculated on the basis of accounting information is present in table 2

Table 2 Derivative indicators

Nr. crt.	Indicators	Notations	2019	2020	Indices of dynamics (%)
1	Financial rate of return (%) $Rrf = Mcp \times Rre$	<i>Rrf</i>	4.1194	5,3847	130.71
2	Economic rate of return (%) $Rre = Vra \times Rrc$	<i>Rre</i>	2.8817	2,6575	92,21
3	Equity multiplier $Mcp = Mai + Mac + Mca$	<i>Mcp</i>	1.4294	2.0262	141.76
4	General financial autonomy rate (%) $Raf = 1/Mcp$	<i>Raf</i>	0.6995	0.4935	70.54
5	Equity multiplier through fixed assets	<i>Mai</i>	1.0533	1.4152	134.35
6	Equity multiplier through current assets	<i>Mac</i>	0.3760	0.6086	161.84
7	Equity multiplier through advance expenses	<i>Mca</i>	0.0001	0.0024	2035.45
8	Commercial rate of return (%) (net accumulation margin rate)	<i>Rrc</i>	7.8950	6,2193	78,77
9	Rotation speed of total assets (number of rotations) $Vra = Pac \times Psa \times Vrs$ $Vra = Pac \times Vrac$	<i>Vra</i>	0.3650	0.4272	117,06
10	Inventory turnover rate (number of rotations)	<i>Vrs</i>	2.0289	2.0902	103.01
11	Proportion of stocks in total current assets (%)	<i>Psa</i>	0.6838	0.6806	99.52
12	Proportion of current assets in total assets (%)	<i>Pac</i>	0.2630	0.3003	114,18
13	Rotation rate of current assets (number of rotations) $Vrac = Psa \times Vrs$	<i>Vrac</i>	1.3875	1.4226	102.52
14	Proportion of gross result in economic result (%)	<i>Prb</i>	0.8397	0.8115	96.64
15	Proportion of net result in gross result (%)	<i>Prn</i>	0.7092	0.7406	104,42
16	Rate of return calculated on the basis of the economic result (%)	<i>Rre (re)</i>	4,0632	3.5880	88,30

An important position in the system of relations within the performance pyramid is held by the equity multiplier indicator, which also highlights the degree

of indebtedness of the economic agent in terms of the ratio between total debt and equity:

The factorial analysis of the rate of financial profitability can be carried out on two levels:

- identifying influences by taking into account the indicators within the performance pyramid;
- determining the role of the leverage effect.

The equity multiplier is also known as the capital financial structure indicator, through which three distinct proportionality ratios can be determined between:

- fixed assets and equity (M_{af});
- current assets and equity (M_{ac});
- prepaid expenses (current regularization assets) and equity (M_{ca}).

The proportionality reports M_{af}, M_{ac} and M_{ca} build us on how to distribute the capital multiplier by types of assets (fixed assets, current and prepaid expenses). Further, it is possible to determine more analytical proportions, taking into account fixed assets by type (tangible, intangible and financial) and current assets by categories (stocks, receivables, short-term investments, cash and bank accounts). the basis of the system of indicators within the performance pyramid, the turnover rate of total assets or the number of rotations of total assets (V_{ra}) is a factor influencing the size of the rate of economic return. Under these conditions, the turnover rate of assets is in turn influenced by the following three factors:

- the turnover rate of stocks expressed by the number of their rotations (V_{rs});
- the proportion of stocks in total current assets (P_{sa});
- the proportion of current assets in total assets (CAP).

The interdependent system of the asset turnover rate indicator according to V_{rs}, P_{sa} and P_{ac} contains as the main element of dynamic influence the stock turnover rate. This requires an increase in the turnover rate of stocks by establishing an optimal level of stocks and increasing turnover. It is also important that the level of inventories in current assets is of a size that ensures the continuity of economic activities in terms of quality and low cost and does not produce supernormative financial assets.

The analysis of the dynamics of the rate of financial profitability considers the determination of the total change of this indicator and the influence of the factors that explain the change, using the method of successive substitutions.

• **Model 1**

$$\Delta = Rrf_1 - Rrf_0 = 5,3847\% - 4,1194\% = 1,2652\%$$

$$\Delta = \Delta M_{cp} + \Delta Rre = 1,4108\% + 1,3550\% = 1,2652\%$$

From which:

a) The influence of changing the equity multiplier:

$$\Delta M_{cp} = (M_{cp1} - M_{cp0}) \times R_{re0} = (2,0262 - 1,4294) \times 2,8817\% = 1,7197\%$$

$$\Delta M_{cp} = \Delta M_{ai} + \Delta M_{ac} + \Delta M_{ca} = 1,0428\% + 0,6702\% - 0,0066\% = 1,7197\%$$

From which:

a₁) The influence of changing the equity multiplier through fixed assets:

$$\Delta M_{ai} = (M_{ai1} - M_{ai0}) \times R_{re0} = (1,4152 - 1,0533) \times 2,8817\% = 1,0428\%$$

a₂) The influence of changing the equity multiplier through current assets:

$$\Delta M_{ac} = (M_{ac1} - M_{ac0}) \times R_{re0} = (0,6086 - 0,3760) \times 2,8817\% = 0,6702\%$$

a₃) The influence of changing the equity multiplier through advance expenses:

$$\Delta M_{ca} = (M_{ca1} - M_{ca0}) \times R_{re0} = (0,0024 - 0,0001) \times 2,8817\% = 0,0066\%$$

b) The influence of changes in the rate of economic profitability:

$$\Delta R_{re} = (R_{re1} - R_{re0}) \times M_{cp1} = (2,6575\% - 2,8817\%) \times 2,0262 = -0,4544\%$$

$$\Delta R_{re} = \Delta V_{ra} + \Delta R_{rc} = 1,3133\% + 0,0416\% = -0,4544\%$$

From which:

b₁) The influence of the change in the turnover rate of total assets:

$$\Delta V_{ra} = (V_{ra1} - V_{ra0}) \times R_{rc0} \times M_{cp1} = (0,4272 - 0,3650) \times 7,8950\% \times 2,0262 = 0,9964\%$$

$$\Delta V_{ra} = \Delta P_{ac} + \Delta P_{sa} + \Delta V_{rs} = 0,8280\% - 0,0319\% + 0,2003\% = 0,9964\%$$

From which:

- The influence of the change in the proportion of current assets in total assets:

$$\Delta P_{ac} = (P_{ac1} - P_{ac0}) \times P_{sa0} \times V_{rs0} \times R_{rc0} \times M_{cp1} = (0,3003\% - 0,2630\%) \times 0,6838\% \times 2,089 \times 7,8950\% \times 2,0262 = 0,8280\%$$

- The influence of the change in the proportion of inventories in total current assets:

$$\Delta P_{sa} = (P_{sa1} - P_{sa0}) \times P_{ac1} \times V_{rs0} \times R_{rc0} \times M_{cp1} = (0,6806\% - 0,6838\%) \times 0,3003\% \times 2,0289 \times 7,8950\% \times 2,0262 = -0,0319\%$$

- The influence of changing the turnover rate of stocks:

$$\Delta V_{rs} = (V_{rs1} - V_{rs0}) \times P_{ac1} \times P_{sa1} \times R_{rc0} \times M_{cp1} = (2,0902 - 2,0289) \times 0,3003\% \times 0,6806\% \times 7,8950\% \times 2,0262 = 0,2003\%$$

b₂) The influence of changing the rate of commercial profitability:

$$\Delta R_{rc} = (R_{rc1} - R_{rc0}) \times V_{ra1} \times M_{cp1} = (6,2193\% - 7,8950\%) \times 0,4272 \times 2,0262 = -1,4508\%$$

Based on the calculations performed, it is found that the rate of financial profitability was higher in the calculation period by 30.71% compared to the level recorded in the base period. The factors that determined this increase can be

assessed as having both a positive influence and a negative impact, as well as factors with a positive influence, but insufficiently capitalized, as follows:

The increase in the rate of financial profitability is explained by the increase of both the equity multiplier, by 41.76%.

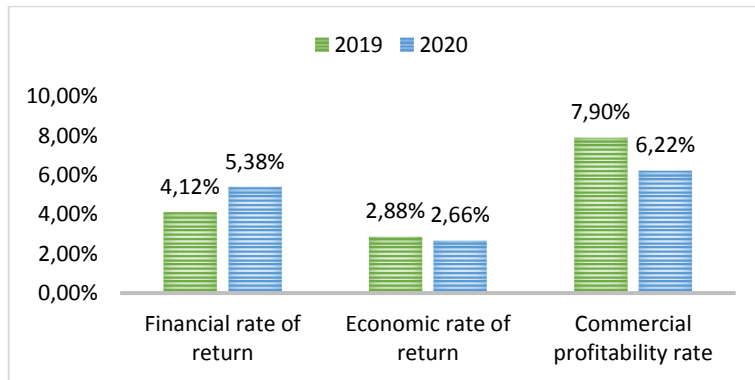


Figure 1 - Evolution of profitability rates

There is a predominant influence of the quantitative factor M_{cp} , with 41.76%, compared to 7.79%, which is the negative influence of the qualitative factor R_{re} , this signaling the need to transform the type of extensive activity into an intensive one, which ensures a efficient and sustainable economic course.

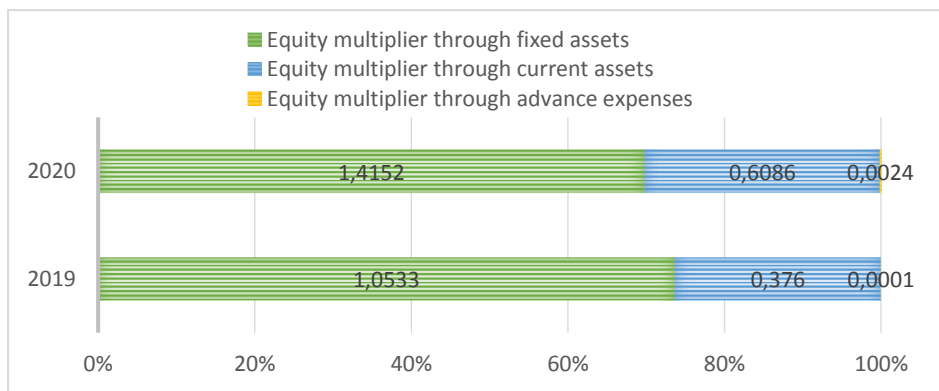


Figure 2 - Effects of the equity multiplier

The equity multiplier establishes the ratio of the total assets or liabilities with the equity, and the inverse form of this ratio, called the general financial autonomy rate, registers a decrease of 29.46%.

The components of the accounting asset contribute to the influence of the change of the equity multiplier on the increase of the financial profitability rate as follows:

- through fixed assets: -14.40%;
- through current assets: 3.12%;

The decrease of equity by 36.28% is preceded by the increase of the value of both current assets, by 3.12%, which demonstrates the decrease of the proportion of debts in total accounting liabilities, the degree of financial coverage from external sources and the capital multiplier.

Financial resources from outside the company (total liabilities) cover a larger part of fixed assets and current assets during the calculation period than the basic one.

The decrease of the economic profitability rate by 7.78%, which materializes in the increase of the financial profitability rate by 30.71%, supports in its turn the following influences:

- increasing the turnover rate of total assets by 17.06%;
- decrease of the commercial profitability rate (net accumulation margin rate) by 21.22%.

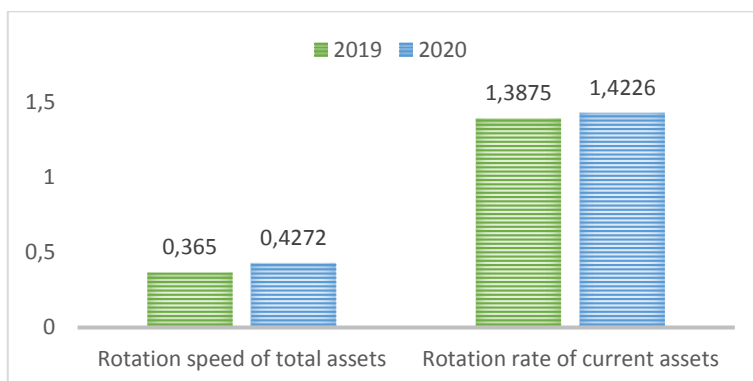


Figure 3 - Asset turnover rate

The increase in the turnover rate of total assets must be seen primarily in terms of the turnover rate of current assets, which has a decrease and an insignificant influence on increasing the rate of financial return by 0.1684% ($\Delta Psa + \Delta Vrs = -0.0319\% + 0.2003\%$).

▪ **Model 2**

$$\Delta = Rrf_1 - Rrf_0 = 5,3847\% - 4,1194\% = 1,2652\%$$

$$\Delta = \Delta M_{cp} + \Delta Prn + \Delta Prb + \Delta Rre(re) = 1,7988\% + 0,2172\% - 0,1720\% - 0,5786\% = 1,2652\%$$

As in:

a) **The influence of changing the equity multiplier:**

$$\Delta M_{cp} = (Mcp_1 - MCP_0) \times Rre_0 = (2,0262 - 1,4294) \times 2,8817\% = 1,7988\%$$

b) The influence of the change in the proportion of the net result in the gross result:

$$\Delta Prn = [(Prn_1 - Prn_0) \times Mcp_1 \times Prb_0 \times Rre(re)_0] \times 100 = [(0,7406 - 0,7092) \times 2,0262 \times 0,8397 \times 4,0632] \times 100 = 0,2172\%$$

c) The influence of the change in the proportion of the gross result in the economic result:

$$\Delta Prb = [(Prb_1 - Prb_0) \times Mcp_1 \times Prn_1 \times Rre(re)_0] \times 100 = [(0,8115 - 0,8397) \times 2,0262 \times 0,7406 \times 4,0632] \times 100 = -0,1720\%$$

d) The influence of the change in the rate of economic profitability calculated on the basis of the economic result:

$$\Delta Rre(re) = [(Rre(re)_1 - Rre(re)_0) \times Mcp_1 \times Prn_1 \times Prb_1] \times 100 = [(3,5880 - 4,0632) \times 2,0262 \times 0,7092 \times 0,8115] \times 100 = -0,5786\%$$

The second model used to analyze the dynamics of the financial rate of return provides us with the following information:

The rate of financial profitability was higher in the calculation period by 30.71% compared to the level recorded in the base period. The factors that explain this state of economic and financial performance are:

- the rate of economic profitability calculated based on the economic result has an influence of -0.5786%;
- the increase of the equity multiplier is 1.7988%;
- the change of the two proportions of the net result in the gross result and the gross result in the economic result has contradictory influences of approximately 0.2172% respectively -0.1720%.

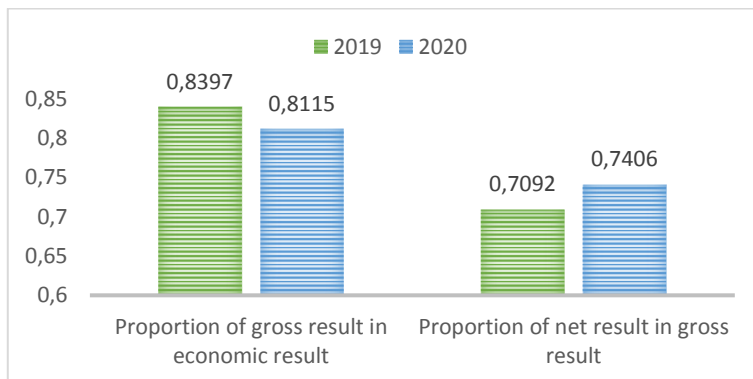


Figure 4 - Proportion of results

Managers who advocate for performance have the chance to act on the basis of the decisions they make in order to correct unfavorable influences, primarily in the direction of a more sustained increase in the rate of economic profitability by

increasing the turnover of total assets, which can be achieved by outpacing the growth of the accounting asset by increasing the net profit. To achieve this result, measures to reduce the relative level of economic expenditure are a priority. In the context of managerial intervention, therefore, the idea of focusing on the factors that had a lower positive influence (economic rate of return and turnover of current assets) and the application of viable, well-founded measures to support the growth rate is also outlined. financial profitability

STUDY 3

Financial management is an essential tool used in the management of an entity and is a main and indispensable activity for any economic activity, not limited to the management of current activities based on financing production and sales. In this context, given that we live in a competitive economy, the competitiveness and efficiency of the activity of any entity is influenced by the ability of managers to implement the principles, methods and techniques of modern financial management.

Events in recent years have shown that the incompetence of managers and erroneous management decisions regarding the management of financial flows have been the basis for the bankruptcy of an economic entity. In this context, starting from the fact that the bankruptcy of a company is caused by the lack of liquidity, it can be concluded that financial management is the one that can influence the success or failure of an entity.

The financial position of an entity represents all the assets and capital over which it exercises control. The analysis of the financial position is performed on the basis of indicators determined using the information in the balance sheet.

Within the agricultural company we will analyze the structure rates of the balance sheet asset for the period 2017-2019. The necessary data were taken from the balance sheets of the company during the analyzed period, being summarized as follows:

As a result of the economic development of economic entities, the economic and competitive environment has experienced a complex development, and in this context, the activity of enterprises has become much more diversified and has required the emergence of new tools and better management techniques to help companies. To overcome the new obstacles that have arisen, which are becoming more and more numerous and costly. With such an approach, the traditional management of enterprises, which was initially based only on the analysis and later on the interpretation of financial-accounting data, proved to be incapable of being used in the evaluation and expression in a more concrete way of the real performance of a company. economic entities.

Table 1 Structure of the assets of the agricultural company in the period 2017-2019

Item name	Analyzed period		
	2017	2018	2019
Fixed assets	2.371.627	1.081.322	838.015
Intangible assets	0	0	0
Tangible fixed assets	2.194.602	880.542	647.177
Financial assets	177.025	200.780	190.838
Current assets	4.466.813	3.003.735	4.438.615
claims	3.958.075	2.291.061	3.640.233
Inventories	474.503	700.623	788.092
Short-term financial investments	0	0	0
Cash	34.235	12.051	10.290
Expenses registered in advance	1.523.766	5.170.322	6.301.958
Total active	8.362.206	9.255.379	11.578.588

Source: Company financial statements

Based on the data from the company's financial statements, I will calculate and analyze the main structure rates of the balance sheet asset:

- Rate of fixed assets - this indicator highlights the share of fixed assets in the total assets held by the company;
- Current assets rate - this indicator shows the share of current assets in the total assets held by the company;

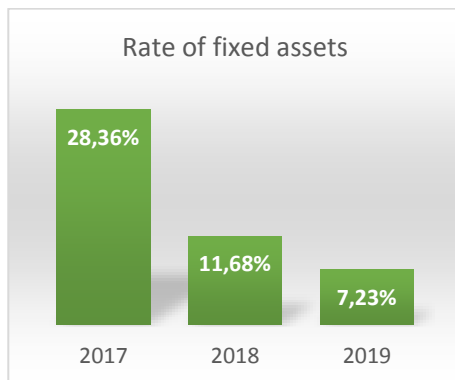


Figure 1 - Rate of fixed assets

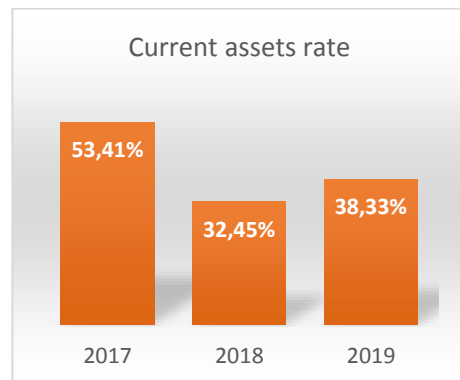


Figure 2 - Current assets rate

Source: Own calculations according to the company's financial statements

It can be seen that in the analyzed period the indicator Asset rate of fixed assets decreased from 28.36% in 2017 to only 7.23% in 2019. This is due to the sale of a land owned by the company.

Regarding the Current Assets Rate indicator, the table shows that its value is oscillating. Thus, we notice that in 2017 the current assets represented 53.41% of the total assets owned by the company, and in the following years the value of this indicator will decrease to 32.45%, respectively 38.33%. This was determined both by the increase in the company's stock volume and by the decrease in the value of receivables.

The analysis of the structure rates of the balance sheet liabilities highlights aspects regarding the autonomy, stability and financial indebtedness of the company. Therefore, these indicators are also known as rates of funding sources.

In order to calculate the specific indicators of the structure rates of the balance sheet liability, in the following table we will summarize the structure of the liability elements of the agricultural company from 2017-2019.

Table 2 The structure of the liabilities of the agricultural company in the period 2017-2019

Item name	Analyzed period		
	2017	2018	2019
Own capital	791.597	949.900	1.124.099
Short-term debt (less than 1 year)	1.137.918	1.888.659	1.546.736
Long-term debt (over 1 year)	5.984.916	5.969.045	8.459.978
Investment grants	0	0	0
Provisions for risks and expenses	447.775	447.775	447.775
Permanent capital (equity + provisions + long-term debt)	7.224.288	7.366.720	10.031.852
Total debts	7.122.834	7.857.704	9.584.077
Advance income	0	0	0
Total Liabilities	8.362.206	9.255.379	11.578.588

Source: Company financial statements

Based on the data from the company's financial statements, I will calculate and analyze the main structure rates of the balance sheet liability:

- Financial stability rate - this indicator reflects the share of stable sources of

financing in the total sources of financing;

- Rate of financial autonomy - this indicator expresses the share of own financing sources in the total financing sources;
- Global debt ratio - this indicator highlights the share of total debt in the total liabilities of the company.

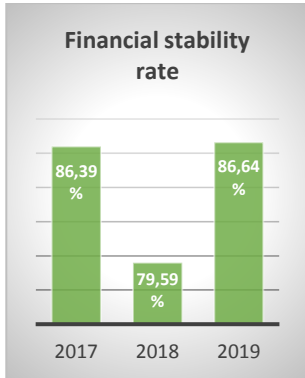


Figure 3 - Financial stability rate

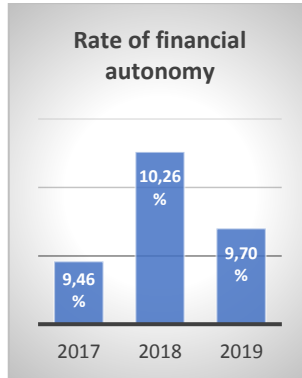


Figure 4 - Rate of financial autonomy

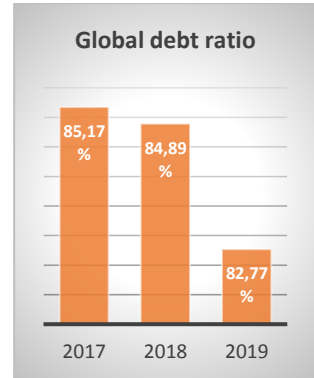


Figure 5 Global debt ratio

Source: Own calculations according to the company's financial statements

According to the calculations made, it is observed that the financial stability rate indicator registered high levels, but relatively stable in the analyzed period, so that the company registered in 2017 a rate of 86.39%, the lowest value being recorded in 2018 of 79.59 %.

Regarding the rate of financial autonomy, the calculations show that the value of the indicator was 9.46% in 2017, and the highest value was recorded in 2018 of 10.26% due to the increase in the value of the company's equity

The increase in the value of this indicator is a good signal for the company and indicates a favorable situation, as there is a higher growth rate of equity in relation to medium and long-term debt. Thus, it should be noted that financial autonomy is paramount for the company because it offers the opportunity to decide freely, or to take out new loans if necessary.

Regarding the indicator of the global debt rate, it is observed that in the whole analyzed period it registered high values, of over 80%. According to the standards, it is recommended that the maximum level of indebtedness accepted, at a bearable degree of risk, be 66%. If this value is higher as recorded by the company throughout the analyzed period, it can be said that the risk of not being able to pay these debts is higher.

From a financial point of view, the balance sheet represents a balance between the resources attracted by the company (capital and debt) and the allocations made (assets). Thus, by analyzing the financial balance of the company, we will reflect the equality relations between the sources of financing and the uses of financial resources. The objective of the financial balance analysis is to provide the information necessary for financial management to make the right management decisions for the company.

To analyze the financial balance of the company we will calculate the following indicators:

- Net income (SN) - this indicator reflects the net worth of shareholders, respectively the non-engaged assets;
- Working capital (FR) - this indicator expresses the part of the equity remaining at the disposal of the company after the financing of the fixed assets and represents the expression of the long-term financial balance;
- Working capital requirements (NFR) - this indicator expresses in the company the short-term balance and presents the situation of the short-term financial needs of the entity compared to the resources attracted in the short term;
- Net Treasury (TN) - this indicator expresses the overall balance of the company, following both the short-term and long-term financial balance. In other words, this indicator is the most relevant expression of a balanced and efficient activity.

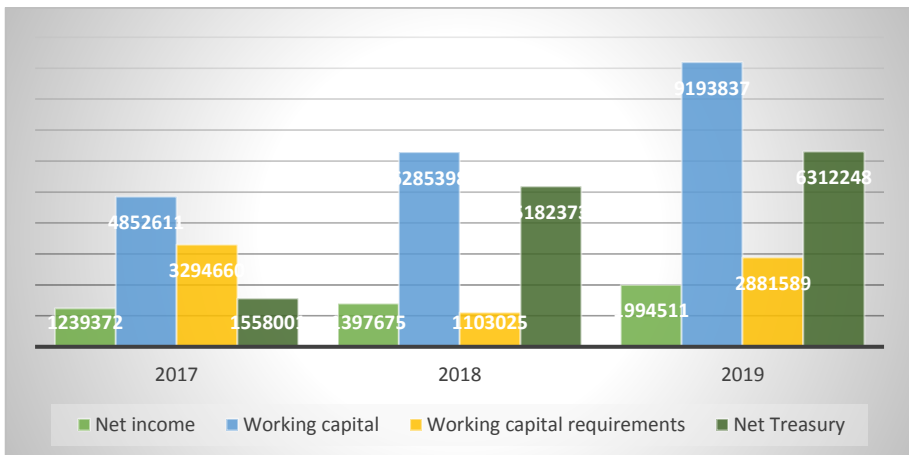


Figure 6 - The financial balance of the company

Source: Own calculations according to the company's financial statements

It can be seen that throughout the analyzed period the indicator net situation registered positive and increasing values, from 1,239,372 lei in 2017 to 1,994,511 lei in 2019. These positive values recorded by the indicator show that at the level of the company there are economically efficient management, and the increase of the value of the indicator in the analyzed period can show an increase of the shareholders' fortune, thus fulfilling the main objective of the financial management [6].

From the calculations made, it is observed that the value of the working capital registered in the analyzed period was increasing from 4,852,661 lei in 2017 to 9,193,837 lei in 2019. This fact is not necessarily beneficial for the company, because a the high value of this indicator implies long-term resources attracted in excess to finance current needs, and long-term resources generate costs for the company, shareholders expecting additional remuneration in the form of dividends, and creditors will receive higher interest. Therefore, in a company, it is recommended that the value of the working capital indicator be as close to zero as possible.

From the calculations made based on the balance sheets of the company it is observed that throughout the analyzed period the value of the working capital requirement was positive, which shows that the company has additional short-term allocations compared to the resources attracted over the same period. Thus, it can be said that the financing of the short-term needs of the company is done either on the basis of working capital or on the basis of short-term loans.

It can be observed that the value of the indicator Net Treasury registered in the analyzed period a significant increase from 1,558,001 lei in 2017 to 6,312,248 lei in 2019. This fact, we

shows that there is a surplus of cash within the company compared to the immediate financial debts, this situation being favorable and desirable, as it expresses the existence of the general balance at the level of the company.

According to the analysis performed, it can be mentioned that in order to achieve financial balance at the company level it is necessary to respect the principles by which permanent allocations, represented by fixed assets, are financed from permanent resources, namely equity and long-term loans due to slower turnover. and temporary allocations, represented by current assets, to be financed on the basis of temporary resources, namely short-term debt. It should also be noted that a higher value of permanent resources than the permanent allocation of funds indicates that the entity has a margin of safety that allows it to cope with unforeseen events [3].

Based on the information held in the company's profit and loss account for the period 2017-2019, the main categories of income and expenses are summarized

as follows:

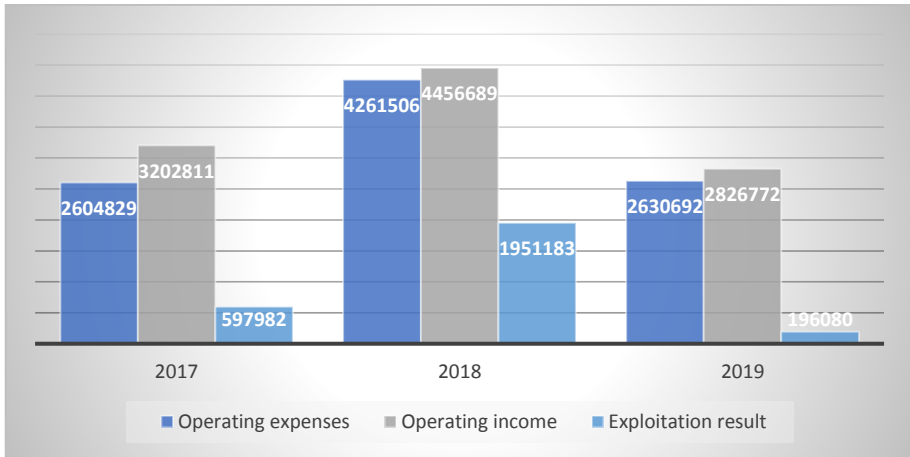


Figure 7 - The result of exploitation

Source: Own calculations according to the company's financial statements

Within the company, operating expenses include expenses for raw materials and materials, expenses for goods, personnel, and in the category of operating income are taken into account turnover, income related to the cost of production in progress, income from revaluation of fixed assets, income from operating subsidies.

Regarding the operating result achieved by the company in the period 2017-2019, it can be seen that it recorded positive values throughout the analyzed period, but had a downward trend in 2018 and 2019 compared to the value recorded in 2017. Positive values recorded shows us that the company carries out a normal current activity.

Another important indicator for analyzing the performance of an entity is the financial result of the company. It expresses the financial activity of the company having in its composition elements related to the financial flows, as well as elements corresponding to the attached risks. This indicator is calculated according to the following relation: $R_{fin} = \text{Financial income} - \text{Financial expenses}$

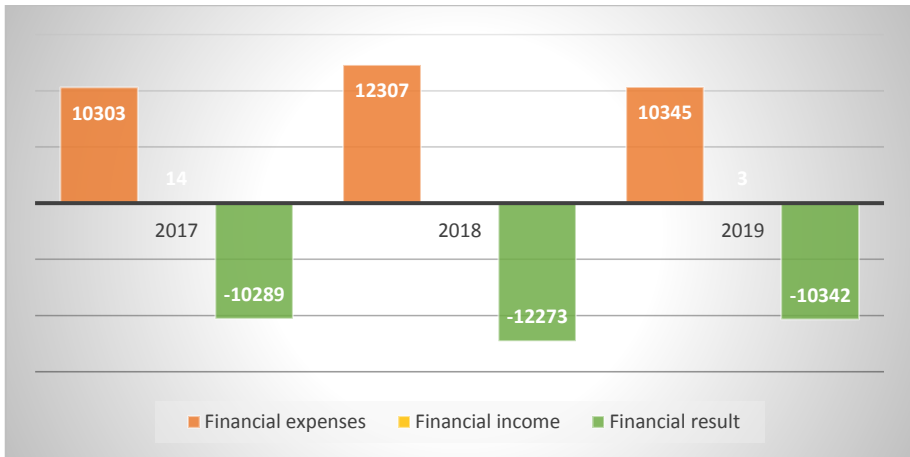


Figure 8 - The financial result

Source: Own calculations according to the company's financial statements

Within the analyzed company, the category of financial expenses includes interest expenses, and the category of financial income includes interest income.

During the analyzed period, it can be seen that the company registered a negative financial result, because the interest paid on the contracted loans exceeds the value of the interest obtained by the company from the financial investments.

Regarding the indicator, the extraordinary result, during the analyzed period, according to the data from the profit and loss account of the company did not record extraordinary income or expenses [7].

The next indicator calculated on the basis of the profit and loss account is the gross result for the year. It takes into account the company's financing policy and combines the operating result with the financial one.

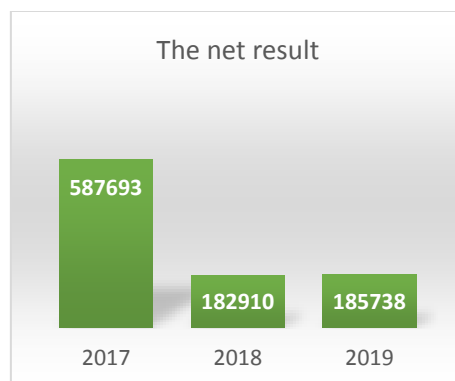


Figure 9 - The net result

Source: Own calculations according to the company's financial statements

To measure a company's performance, another indicator to follow is the net result for the year. It highlights the final result of a company after the payment of income tax.

The calculations show that throughout the analyzed period the company recorded a net result of the positive year, but on a downward trend, which shows us that the entity recorded a profit and the total activity of the company is a profitable one.

Another set of indicators that present the financial situation of an entity are economic profitability and financial profitability. These indicators express the ability of the economic entity to generate profit.

The rate of economic return on assets (ROA) expresses the efficiency of the material elements engaged in the company's activity. Economic profitability measures the degree of profitability of using the total asset and is calculated according to the following relationships:

$$\text{ROA} = \text{Gross Profit} / \text{Total Assets} * 100$$

The rate of financial return (ROE) expresses the appreciation of the efficiency of the capital investments of the shareholders and the opportunity to maintain them and can be calculated as a ratio between the net result of the financial year and the own capital:

$$\text{ROE} = \text{Net Profit} / \text{Equity} * 100$$

Within the company, we calculated the economic profitability and the financial profitability for the period 2017-2019, the results being expressed in the following.

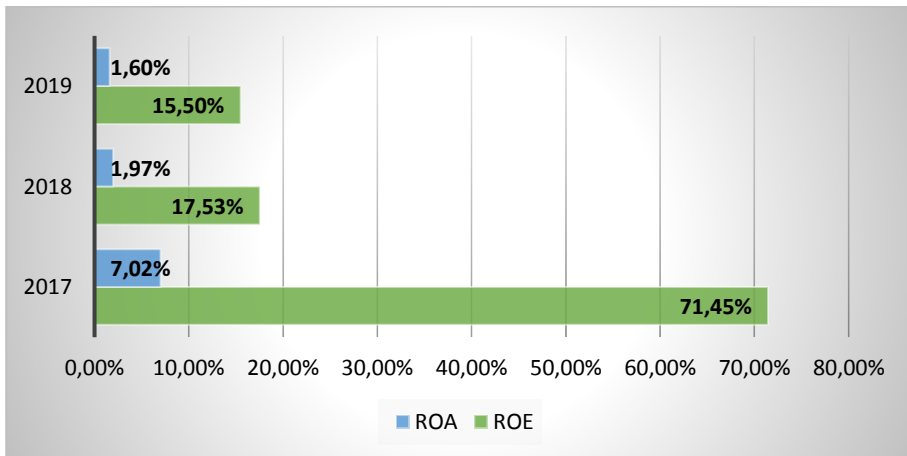


Figure 10 - Evolution of profitability indicators

Source: Own calculations according to the company's financial statements

Regarding the economic profitability indicator, the calculations show that its value registered a downward trend in the analyzed period, its value decreasing from 7.02% in 2017 to 1.6% in 2019. This decrease was determined by on the one hand by the decrease in the value of the profit, and on the other hand by the increase of the value of the total assets.

Regarding the financial profitability indicator, we also notice that there is a decrease from 71.45% in 2017 to 15.5% in 2019. This evolution is determined by the decrease in the value of profit in the analyzed period and the increase in the value of equity.

At present, financial management has experienced a strong development, this being an indispensable component for any economic entity.

Financial management is essential and must know in detail the cost of financing, so as not to lead the company to financial problems, or even bankruptcy. Thus, through financial management activities it is necessary to better forecast future revenues in order to determine the extent to which they can cover the expenses necessary for the normal operation of the company.

Regarding the analysis of financial management within an economic entity, we conducted a study on the financial position of the company which highlighted its importance for all categories of users and especially for current and potential investors, but also for financial creditors. Thus, we conducted an analysis of the structure of the company's assets by calculating a number of efficient indicators to suggest the company's situation in the period 2017-2019. These indicators show us concretely the situation from certain points of view of the economic entity and in a correlated way, they express the way in which it evolves from one period of time to another.

Within the company we analyzed the financial performance based on the profit and loss account for the period 2017-2019, by calculating and analyzing indicators based on the company's profitability and we aimed to establish the results obtained by using the factors of production.

The analysis of financial performance indicators is of particular importance within an entity, primarily for the financial manager, because based on them it is expressed how the company's profit is formed, as well as possible financial difficulties registered at the company level and the causes that determined the appearance. them.

According to the analysis performed, it can be mentioned that in order to achieve financial balance at the company level it is necessary to respect the principles by which permanent allocations, represented by fixed assets, are financed from permanent resources, namely equity and long-term loans due to slower turnover. and temporary allocations, represented by current assets, to be

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2022

ISBN 978-80-8185-045-5