THE VALUATION AND ACCOUNTING OF TRADE RECEIVABLES

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Abstract: Regardless of their field of activity, a problem frequently faced by Romanian companies is that of the valuation and accounting of trade receivables. This article focuses on two types of valuations of trade receivables: the first one is their accounting valuation, and the second is the valuation of the receivables on the occasion of the overall company valuation. We also present accounting and fiscal aspects related to recording receivables in the company accounting records, including their reversible impairment.

Key words: trade receivables, valuation, accounting, company valuation, reversible impairment

INTRODUCTION

Currently, economic information plays an essential role in all fields of activity. The main data source of the economic information system is accounting, whose scope is the company. For the achievement of the company object of activity, legal and patrimonial relationships with a multitude of legal entities and natural persons are necessary. These relationships give rise to obligations and rights of claim with direct influence on the size and structure of the company assets. In my opinion, a detailed analysis, from multiple points of view, of the valuation and accounting of trade receivables, which can be found in the financial position of most companies, will contribute to the increase in the quality of the accounting information for the appropriate substantiation of the decision made by the information users.

MATERIALS AND METHODS

As highlighted in the specialised literature guiding the accounting research methodology [1, pp.17-18], in the accounting field, the research is focused on what the researcher and the professional accountant do, or should do, under conditions specific to the regulations or standards adopted in a country in relation to their professional activity, or at the level of a group of associated countries or recognized organizations. The accounting research should be understood as an investigation activity carried out with the purpose of improving communication between the users of the treasure of accounting knowledge/information and the society in order to continuously improve the accounting practice. This article is based on quality research methods, more specifically:

- The research of the practice in the field (aiming to contribute to the knowledge of the issues faced by the professional accountant in a certain problematic hypostasis during his activity);
- The case study research (which implies the investigation of a contemporary phenomenon in its context).

The main objectives of the study are:
- To highlight the method of valuating trade receivables in accounting;
- To outline the fiscal implications of accounting trade receivables;
- To highlight the role of the analysis of the clients’ management in the company valuation process;
- The accounting treatment of trade receivables in the consolidating the accounts of the groups of companies
- To present the method of valuating trade receivables on the occasion of the overall valuation of the company.
RESEARCH RESULTS

In any company, a fundamental dimension is value: “The greatest of all gifts is the power to estimate things at their true worth” [4, p. 37]. Value is not a certitude, it is an opinion about how much goods and services are worth at a certain moment, according to a certain definition of value.

Trade receivables and trade payables reflect the relationships of the company with other companies in relation to the goods and services supply and sale. Trade receivables reflect the rights of the company towards other legal entities or natural, determined by the sale of goods, completion of works or provision of services, for which it must receive a value equivalent or a consideration. For the accounting of the settlement relationships between the seller and its customers, in the seller’s accounting, accounts in the 41 group “Customers and similar accounts” from the Chart of accounts:

- 411 Customers
  - 4111 Clienți
  - 4118 Doubtful customers or customers involved in litigation
- 413 Bills of exchange receivable
- 418 Customers - invoices to be issued
- 419 Advance payments from customers.

Account 419 “Advance payments from customers” is included in the group of accounts analysed, which has an economic content of debt and an accounting function of liability, conversely compared to the other accounts in the same group, which accounts are receivables and implicitly assets. The hereinabove mentioned accounts receivable have a few common characteristics, the most significant being the following:

- They are accounts of current assets that are to be settled, with an accounting asset function;
- They reflect at debt the invoicing price, including the corresponding VAT for the sale of goods, provision of services and completion of works;
- They are balance sheet accounts, and the debit balances they can have are related to uncollected receivables;
- The amount of the final debit balances existing at the end of the accounting period, diminished with the value adjustments for temporary impairment corresponding to the debts in question, is entered in the balance sheet assets, in the current assets group (B), sub-group “Claims”;
- The analytical accounting is organized on categories of receivables, as well as on each natural person or legal entity. The accounting of trade receivables in a foreign currency is kept both in RON and in the respective foreign currency. Customers are also grouped into domestic and foreign, and within each of these categories, receivables are delimited according to their due date. Also, claims generated from the transactions with property reserve clause, and those related to the beneficiary units where suppliers own equity interests.

In relation to the nature of the assets, the direction of the movements occurred in the assets and the time when the valuation is made, the following rules and forms of valuation are highlighted: valuation at the entry in the assets, valuation at exit from the assets, valuation at inventory, and valuation at balance sheet.

- **Valuation at the entry in the assets**

  Receivables are valued at nominal value recorded in the documents, i.e. the amounts to be received. Receivables recorded in a foreign currency and those recorded in RON, whose settlement is made in a foreign currency, resulted as an effect of transactions, are bookkept both in RON, at the exchange rate of the day when the operations are made, communicated by BNR (National Bank of Romania), as well as in the foreign currency.
At the end of each month, receivables and payables in a foreign currency are valuated at the exchange rate of the foreign exchange market, communicated by the National Bank of Romania in the last banking day of the respective month. The foreign exchange differences recorded are recognized in the accounting at incomes expenses from foreign exchange differences, as the case may be. For the first day of the month, both transactions performed in a foreign currency, as well as the monthly valuation at the exchange rate of the National Bank of Romania are accounted for, using:

a) for the accounting of the transactions performed in the last day of the month, the exchange rate of the foreign exchange market, communicated by the National Bank of Romania, in the last banking day before the operation;

b) the exchange rate of the foreign exchange market communicated by the National Bank of Romania, in the last banking day of the respective month, for the valuation of receivables and payables in a foreign currency, the foreign currency cash and other cash values, such as treasury bills in a foreign currency, letters of credit and deposits in a foreign currency, present in the balance at the end of the month.

These provisions are also applicable to receivables and payables recorded in RON, whose settlement is made depending on the exchange rate of a foreign currency. In this case, the differences recorded are recognized in accounting at other financial incomes or other financial expenses, as the case may be.

For example, we suppose that SC Iatsa SA sells finished products to another customer in Greece, at the selling value mentioned in the invoice, of 4,000 eur. Both companies are VAT payers, and the company in Greece supplied the VAT registration number of the company in Romania. The EUR exchange rate, set by BNR on the delivery date is 4.4774 RON/EUR.

Under the tax regulations, this operation falls into the scope of intracommunity deliveries, in the exempt operations, and the invoice issued mentions “reverse taxation” (if the customer had been from an intracommunity country, for example in Turkey, no VAT is charged on sales, as the export is a tax-exempt operation).

| 7015 Income from the sale of finished products | 17,909.6 RON (4000 eur* 4.4774 RON/eur) |
| 4111 Customers | |

At the end of the month in which the receivable was recorded, the eur exchange rate communicated by BNR is 4.4721 RON/EUR. SC Iatsa registered the present value of the receivable in the foreign currency:

| 665 Expenses from exchange rate differences | 4111 Customers |
|  | 21.2 RON (17909.6-17888.4*) |

*the receivable present value is 4,000 eur*4.4721 RON/euro =17,888.4 RON. The receivable present value decreases compared to the initial value, consequently, unfavourable exchange rate differences will be recorded.

○ Valuation at exit from the assets

When receivables are collected, consequently, when their value is deducted from the accounting, or, in other words, when they are eliminated from the assets, they are used at their nominal value present in the accounting, called original cost.

The exchange rate differences occurred on the occasion of settling receivables and payables in a foreign currency at rates that are different compared to those initially recorded during the month or as compared to those recorded in accounting must be recognized in the month when they appear, as incomes or expenses from exchange rate
differences. When the receivable or the payable in a foreign currency is settled during the same month when it occurred, the entire exchange rate difference is recognized in that month. When the receivable or the payable in a foreign currency is settled in a subsequent month, the exchange rate difference recognized each month, occurring before the settlement month, is determined taking into account the modification of the exchange rates occurred during each month. The value differences occurred when receivables and payables in RON are settled, depending on an exchange rate different from the one at which they were recorded initially during the month or from those at which they are recorded in the accounting must be recognized in the month when they occur, in other financial incomes or expenses.

If we assume that the company Iatsa SA (for which I exemplified the product sale), records the collection of the receivable by bank transfer, within 20 days from the moment when it is discounted, the foreign exchange rate communicated BNR when the receivable is collected is 4.4749 RON/eur. The accounting for the receivable by bank transfer is as follows:

<table>
<thead>
<tr>
<th>5124 Cash at bank in foreign currencies</th>
<th>%</th>
<th>17 899.6 RON</th>
</tr>
</thead>
<tbody>
<tr>
<td>4111 Customers</td>
<td></td>
<td>17 888.4 RON</td>
</tr>
<tr>
<td>765 Incomes from exchange rate differences*</td>
<td></td>
<td>11.2 RON</td>
</tr>
</tbody>
</table>

*The exchange rate when the receivable is collected is bigger in the respective moment than when the receivable is discounted, consequently, there are favourable exchange rate differences (financial incomes).

**Valuation at inventory and presentation of the receivables in the balance sheet**

At inventory, receivables are valued at their probable value to be collected. For negative differences found between the inventory value and the book value, adjustments are made for the depreciation of the receivables, while for doubtful receivables adjustments are made for impairment. Receivables in a foreign currency and those settled in RON depending on the exchange rate of a foreign currency, are valued at the exchange rate published by BNR on the day when the accounting period is closed. In the balance sheet, the value of the receivables is diminished by the adjustments for impairment.

For example, if SC Iatsa has recorded in its accounting records a trade receivable with a book value of 1900 RON, and the present (inventory) value represented by the probable value to be collected is 1720 RON, the difference of 180 RON will be accounted for, according to the principle of prudence, as a temporary impairment of value in the form of a value adjustment for the impairment of thereceivable.

| 6814 Operating expenses related to the adjustments for the depreciation of current assets | 491 adjustments for the depreciation of receivables - customers | 180 RON |

According to the fiscal regulations, expenses related to the adjustments for the impairment of receivables, recorded according to the applicable accounting regulations, are deductible within the limit of a percentage of 30% of their value, if the receivables meet the following conditions at the same time:

1. they are not collected in a period that exceeds 270 days from the day of the due date;
2. they are not guaranteed by another person;
3. they are owed by a person that is not affiliated to the taxpayer;
The receivable will be presented in the balance sheet at the value of 1720 RON (final balance due of account 411 in the amount of 1900 RON minus the final credit balance of account 491 in the amount of 180 RON).

We will analyse below, based on the accounting regulations in force and on the specialized materials [7] the commercial and financial discounts used business partners in the supply and sale activities, with an impact on the accounting of the trade receivables and payables.

Discounts granted for stock sales or service provisions that can have a commercial nature (rebates, deductions and volume discounts) or a financial nature (settlement discounts). Commercial and financial discounts are granted in compliance with the general delivery and settlement conditions set between the parties.

Trade discounts granted by the supplier and mentioned on the original invoice decreases the purchase cost of goods. In order to identify the accounting treatment of trade discounts, we should analyze the moment when they are received/granted. In practice, two cases are possible:

- Discounts granted by the supplier and recorded on fiscal purchase invoices. These discounts adjust the purchase cost by reducing it. These trade discounts will not be recorded separately in the accounting records, they simply adjust the purchase cost. Thus, at the buyer, stocks will be recorded at their net commercial value, while at the seller, receivables and implicitly the related incomes will be recorded at the value resulted after decreasing the trade discount. Stocks are written off by the seller at the book value, without taking into account the value of the trade discount granted when they are sold;
- Trade discounts received after invoicing, or granted after invoicing, regardless of the period they are related to, are recorded separately in the accounting records (account 609 “Trade discounts received”, respectively account 709 “Trade discounts offered”), on behalf of third party accounts.

Financial discounts received from the supplier are incomes of the accounting period regardless of the period they are related to and are recorded in account 767 “Discounts received”. At the supplier, such discounts granted are expenses of the period, regardless of the period they are related to, and are recorded in account 667 “Discounts granted”, thus diminishing the value of the original receivable.

For example, SC Iatsa SA sells goods, based on an invoice, to a domestic customer, at a selling value of 3000, with 20 % VAT. They grant to this customer, when they issue the invoice, a 1% trade discount (rebate)

The selling operation is recorded as follows in the accounting records:

<table>
<thead>
<tr>
<th>Account</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>4111 Customers</td>
<td>3,564 RON</td>
</tr>
<tr>
<td>707 Sales of goods</td>
<td>2,970 RON</td>
</tr>
<tr>
<td>4427 Output VAT</td>
<td>594 RON</td>
</tr>
</tbody>
</table>

If the discount was granted after invoicing, the accounting records would be:

- recording the sale of goods based on the original invoice

<table>
<thead>
<tr>
<th>Account</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>4111 Customers</td>
<td>3,600 RON</td>
</tr>
<tr>
<td>707 Sales of goods</td>
<td>3,000 RON</td>
</tr>
<tr>
<td>4427 Output VAT</td>
<td>600 RON</td>
</tr>
</tbody>
</table>
-the invoice is recorded after the recording of the trade discount

\[
\begin{align*}
709 \text{ Trade discounts offered} & \quad \text{36 RON} \\
4427 \text{ Output VAT} & \quad \text{30 RON} \\
4427 \text{ Output VAT} & \quad \text{6 RON}
\end{align*}
\]

We suppose that, after granting the trade discount, the company Iatsa grants a 2%, financial discount (settlement discount) because the customer wishes to pay earlier. This discount is accounted for as follows:

\[
\begin{align*}
667 \text{ Discounts granted} & \quad \text{71.28 RON} \\
4427 \text{ Output VAT} & \quad \text{59.4 RON} \\
4427 \text{ Output VAT} & \quad \text{11.88 RON}
\end{align*}
\]

The valuation of trade receivables at the overall company valuation (for various reasons, such as merger with another company, selling the company, etc.) is necessary only when out of the approaches recognized in valuation, the asset approach is applied. The most general grouping of the approaches used with the purpose of determining the value of a company (with the methods of each approach) takes into account:

**Figure 1. Approaches used in the company valuation and methods comprised in them**

In the case of the application of the methods recorded in the asset-based approach, the valuation of all assets and liabilities of the company is made, in other words, the valuation of all asset and liability items, including trade receivables.

From the valuation point of view, receivables (short-term receivables from customers and other debtors, etc.) are liquid current assets resulted from the credit, wholesale or retail sales. As highlighted in the specialized literature [5, pp. 253-254], we can notice that the treatment of the valuation of the receivables is different depending on the size of the enterprise. In the case of big enterprises, all its receivables are taken into
account, while in the case of small enterprises, the owner will collect the receivables by himself without transferring them to the future owner.

If there is a risk of doubtful customers, the receivables will constitute the object of a separate valuation. Consequently, it is necessary to group and rank customers based on the “payment day” criterion, in order to detect the default risk. The value level of the receivables will thus be diminished, according to the period of delay of the payment of the receivable in question.

### Table 1

**Grouping and ranking customers based on the “payment day” criterion**

<table>
<thead>
<tr>
<th>Decreasing the value level of receivables (%)</th>
<th>Collection delay (days)</th>
</tr>
</thead>
<tbody>
<tr>
<td>10%</td>
<td>31-60 days</td>
</tr>
<tr>
<td>20%</td>
<td>61-90 days</td>
</tr>
<tr>
<td>30%</td>
<td>91-120 days</td>
</tr>
<tr>
<td>100%</td>
<td>More than 120 days</td>
</tr>
</tbody>
</table>

We suppose that the trading company Iatsa SA initiates a company valuation process with the purpose of determining the market value of its shares, and the valuer decides to apply the “The adjusted net asset method”, which falls into the category of the asset-based approach methods. After studying the situation of the receivables at the above-mentioned entity, I will present below the main types of trade receivables and the recovery degree, more specifically, the estimated possibility of collecting them:

### Table 2

**Types of trade receivables and collection terms**

<table>
<thead>
<tr>
<th>Main trade receivables, on collection terms as at 31.12.2015</th>
<th>Value of the receivables -RON-</th>
<th>Receivables to be collected within the term and after exceeding the term -RON-</th>
<th>Within normal collection term</th>
<th>Collection delay</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>31-60 days</td>
<td>61-90 days</td>
</tr>
<tr>
<td>Trade receivables</td>
<td>1,265,244</td>
<td>939,733</td>
<td>130,204.4</td>
<td>65,102.2</td>
</tr>
<tr>
<td>Customers (4111)</td>
<td>651,022</td>
<td>325,511</td>
<td>130,204.4</td>
<td>65,102.2</td>
</tr>
<tr>
<td>Bills of exchange receivable (413)</td>
<td>370,490</td>
<td>370,490</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Customers - invoices to be issued (418)</td>
<td>243,732</td>
<td>243,732</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

The value of the trade receivables in the valuation report will be:

\[939,733 + 130,204.4 - 10\% \times 130,204.4 + 65,102.2 - 651,022 \times 20\% + 97,653.3 - 32,551.1 \times 30\% + 325,511.1 - 325,511.1 \times 100\% = 1,177,356.03 \text{ RON}.

In conclusion, the adjustment of the trade receivables in the valuation report will be “-87,887.97 RON”.

Another important aspect is that of the accounting treatment of the trade receivables in the **process of consolidating the accounts of the groups of big companies**. The companies that are members of the group can carry out economic and financial operations with third parties outside the group and also with other companies within the group (intra-group transactions). If the equivalent value of the goods sold, services provided/works performed is not paid by the end of the accounting period, the companies involved will have mutual payables and receivables recorded in their individual balance sheets. These mutual receivable and payable accounts must be eliminated (depending on the consolidation method applied to each entity involved, in order to prevent the artificial
increase in the group’s receivables/payables), after the inventory and homogenization of the intra-group transactions with the purpose of eliminating them.

CONCLUSIONS

In the current economic environment, where commercial credit between the partners of economic and financial transactions plays an essential role, in my opinion, regardless of their scope, companies record within their current assets significant trade receivables. As can be seen from the review of the theoretical and practical studies presented, the valuation and accounting of trade receivables is complex and implies, in addition to thorough knowledge of the accounting/fiscal regulations, the use of professional judgement.

In the case of an overall company valuation, the assessment of the value of the trade receivables is necessary only if, out of the approaches recognized in valuation, the asset-based approach is applied. Consequently, the valuer authorised to complete the company valuation mission must assess the probability of not collecting its receivables. It is recommended that this assessment should be made based on the statistical information of the company, from the previous accounting periods, concerning the default risk. Thus it is deemed that, based on the previous experience, there is the same probability to collect the receivables recorded in the accounting records of the company as at the valuation day. In the case of a company diagnosis as well, which precedes the actual company valuation, it is useful to analyse the customers’ management by means of the number of turnovers of the receivables through the turnover, or the duration in days of a turnover. This analysis carried out within the commercial diagnosis will provide the valuer with essential information on the value and evolution of the trade receivables of the company and especially on their average collection period.

If the parent company of a group of companies is required to prepare annual consolidated financial statements, in the case of the existence of mutual accounts, for example mutual receivable and payable accounts, under certain circumstances, it is necessary to eliminate such accounts in order to prevent the artificial increase of the receivables and payables of the group taken into account as single, individual entity, in its consolidated balance sheet. Consequently, it is recommendable to use analytical accounts for the presentation of the intra-group transactions in the individual accounting records of the companies involved and to perform an appropriate homogenization in order to eliminate them.

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