

CRITICAL ANALYSIS OF THEIR RISK FINANCIAL INSTRUMENTS

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Abstract:

In the last decade, accounting for financial instruments has experienced a revolution, following the publication of accounting rules on recognition and measurement of these instruments saddle. Need to develop standards for financial instruments appeared on the background of explosion using derivatives and the markets in which they are traded, and as a result of numerous financial scandals that rocked developed countries in the last decade. These were based, among other causes, improper use of derivatives and hiding their disastrous effects of poor management by keeping them off balance and failure to provide related information in the notes of the financial statements.

Key Words: balance, financial statements, stocks, bonds

JEL Classification : M40, M41

Burdened with derivatives on the balance sheet as assets or financial liabilities and impose detailed description of the financial risks relating to fair value, nature and the contractual terms of the financial instruments, risk management policies relating to them.

With regard to the necessary and expected development of the Romanian capital market, domestic firms will use more often in financial instruments. But their accounting, presentation and disclosure of information relating to the individual or consolidated accounts and the impact of their use on the performance and financial position of the entities are very current topics Romanian accounting professionals. [1]

The complexity of the new rules contained in IAS standards - 39 "Financial Instruments , Recognition and Measurement " , has generated heated debate and challenged practitioners involved in the training and preparation of financial statements for the application requirements on:

- Recognition of all derivatives on the balance sheet ;
- Evaluation of many of the financial statements at fair value ;
- Met criteria for cancellation of recognition or use special accounting treatment applicable to operations to protect against financial risk, was, in most cases, entirely new.

Globalization of financial markets has had an impact of the various not spared accounting. The emergence of new financial instruments and the extraordinary development of existing ones imposed the need for accounting standards to reflect the economic and financial reality and calling more frequent financial markets and their products, in order to finance its activities, invest or protect against risks. [3]

Trade liberalization induced but another aspect of globalization, the financial, manifested by financial ties between countries and therefore the free movement of capital. The result was the significant increase in the role and importance of international capital markets. The financial resources needed to develop core business began to be acquired in a growing proportion by transnational companies on the global financial markets, corporations are redirecting from operations expansion capital made in the field of exports or direct investment , for financial transactions primary products (shares, bonds) and derivatives (forward, futures, swaps, options, etc.).

Financial markets have experienced a spectacular development and integration trend can be explained by economies from profound changes due to factors such as disintermediation between prisoners and those who borrow, deregulation of trade and money and on interest rates, allowing the forces market work, the development and spread of new information technologies and lastly but not the most important financial innovations, volatilization occurs in response to interest and exchange rates, which is considered as the driving force behind their development, and due to the need of new sources of financial statements.

In the context of instability that characterizes the international markets, the primary instruments (stocks, bonds, receivables) proved to be ineffective in the face of risk.

Therefore, it was necessary to the emergence of new financial instruments called "derivatives" more sophisticated and harder to use. Subsequently they have diversified, currently there are over 1,200 types of derivatives that are the result of changes in the characteristics of existing financial products or the continuation of existing features in a new product. Futures, options and swaps have become the standard means of hedging, gaining significant popularity among operators, allowing them to take their own risks or transfer them to third parties.

There were so derivative markets had the effect not only reduce financial risks, but also increase the possibilities of obtaining profits from speculating on future events.

Derivatives are today an integral part of risk management policies implemented by large entities around the world. Among the companies that use derivatives, almost 92 % go to them to lay hold hedge rate, a percentage is low to protect against currency risk, the risk of a price change various goods and price fluctuation risk their operators.

Aware of the gravity effects risks can have on their business, managers of the various entities initiate procedures more complex risk upstart or redress the consequences. Hedging (cover) is currently the most used technique to those who risk averse and want to transfer it to another party. It is through derivatives whose value fluctuations outweigh the financial assets and financial liabilities held by the company and is dealt with extensively in technical accounting standards.

Until the advent of IAS - 39, most derivatives were considered off-balance sheet items. The consequence was that their risks could be easily concealed and hidden shareholders and investors, and the lack of a rigorous control, this could cause huge losses or even bankruptcy of the companies that use them inappropriately.

This situation led to normalization accounting bodies (FASB and IASB) introduce strict rules on derivatives and their use for risk management.

The most important provisions were those related to derivatives recognized in the balance sheet as assets and not as historical cost. [2]

The solution of the accounting standard setters was to introduce risk hedge accounting, which is desired by artificial volatility of the results generated by marking to market.

Marking to market, synonymous with the fair value measurement of derivatives, mean and high volatilization results in the profit and loss developments in oscillating markets these instruments in recent years. This special accounting treatment applicable to transactions involving derivatives hedging allows for efficient coverage, offsetting losses in profit and loss in earnings on derivatives and gains by postponing their induction in equity and not in account the result. As the term is too general hedging, accounting standard setters have preferred the use of other terms - hedge accounting. Thus, from an accounting perspective, hedging involves the designation of one or more hedging instruments so that their change in fair value to offset, in whole or in part, changes in fair value or cash flows of a hedged item. [4]

Hedges are an enterprise that protects against risks, in whole or in part, by a second transaction that generates opposite effects of the first transaction in the same risk.

Risks hedged position and the cover are opposite, which makes their related gains and losses to offset.

It can be shown that this type of accounting is the systematic recording and symmetrical changes in value of the hedging instrument and the clouds.

The terms "hdging " and " hedge accounting " differs essentially in that first considers the risks change , the result of business decisions , while the second changes the accounting for gains and losses , representing a accounting decision .

The most important limitation in applying accounting treatment specifically refers to the effectiveness of hedging transaction. This is defined by IAS - 39, paragraph 9 , as the degree to which changes in fair value or cash flows attributable to a hedged risk are offset by the hedging instrument . [5]

According to the IAS - 39 and FAS - 133, efficiency must be very high . In essence, hedging sites economically efficient, but which do not fall within the high economic efficiency (80-125 %) , the rules do not apply hedge accounting operations . It may be noted that any type of receiving hedge accounting treatment special. But the recognition, in some cases, the effective part of the hedge in equity and the ineffective income statement volatility increases significantly the balance sheet and profit and loss account. The changes introduced by IAS - 39 involves not only various professional reasons, but an informational support appropriate management strategies to support hedging. In this context, the restrictions have the effect of reducing the volume of hedges . [5] Therefore, businesses have had to turn to less sophisticated derivatives as hedges accounting rules are easier to apply. Key elements of a hedging relationship the risks are hedged item and the hedging item.

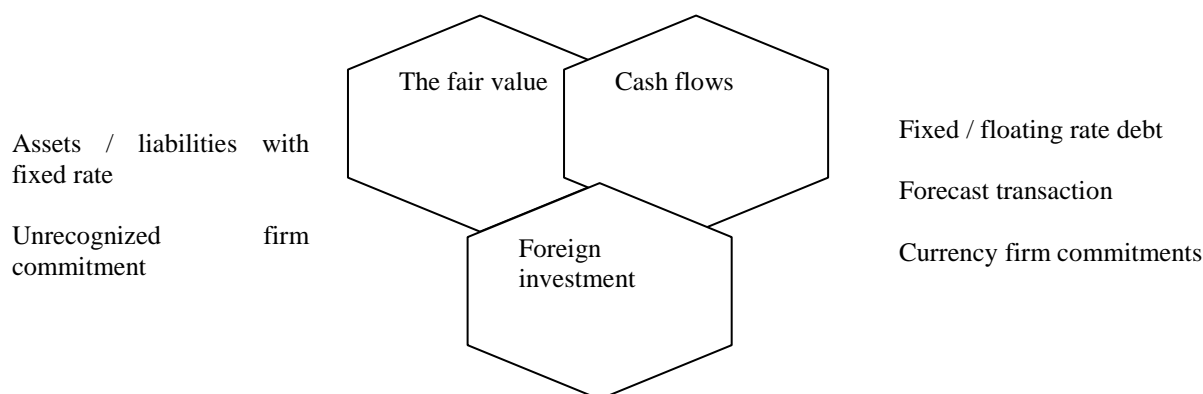
The most significant limitation to the application of the hedge accounting transactions is related to the effectiveness of their coatings, which must be very high.

It is measured based on two types of texts:

- Prospective tests conducted at the beginning of the hedging relationship at each balance sheet date , the duration of the operation;

- Retroactive tests conducted at each financial reporting date, throughout the duration of the hedging operation in accordance with the methodology set out in the documentation. Hedging relationships are classified in accounting terms, the following:
- Fair value hedge - the risk is given by the change in fair value of an asset or liability held, which will affect profit or loss;
- Cover cash flow (cash flow hedge) - the risk is given by the potential volatility of future cash flows, affecting profit or loss;
- Coverage of net investments in foreign entities - this is dealt with in IAS - 21 "Effects of changes in foreign exchange rates" which imposes requirements for using hedge accounting where hedge exchange rate risk for the holdings in such an entity.

The three types of hedging transactions are presented below (fig.nr.1)



In terms of economics, in a hedging relationship are important risk achieving offsetting and reducing exposure. The economic effects of such operations is the same, regardless of the type of financial risk covered.

Conclusion:

The consequences of different accounting according to the classification of operations in one of the three categories. In conclusion, we believe it is justified to be mentioned that according to the policy adopted by the company, the risks to which they are exposed are different and hence disclosures in the financial statements are different.

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