

FINANCIAL ACCOUNTING APPROACHES OF THE REVOLVING LOANS WITH THE EXAMPLE OF THE FOREIGN TRADE COMPANIES

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Abstract

In the current economic context, with a major increase in the foreign business of the Romanian companies, there is a need to finance their activities from various sources in order to meet competition.

For this reason I aimed, with this paper, to identify the way to finance current business of foreign trade companies. Considering that for the majority of foreign trade transactions settlement is performed after a maturity established by agreement between the partners, in this interval various payment obligations may occur, reason for which companies resort to short-term funding sources, usually of the revolving type.

This paper presents on one hand the financial features of two forms of crediting current activity, most often contracted by companies engaged in foreign trade, as the credit line and the global working loans. In the case of the credit line we presented the accounting methodology applicable to a company that engaged in foreign trade, with the purpose of highlighting the accounting peculiarities of the records of the currency credit line, as well as the costs (interests, fees) these imply.

Keywords: credit line, revolving, global working loans, cash-flow, accounting approach, difference in the exchange rate.

JEL classification: M40, M41, G20.

1. Introduction

The financing of current activity aims to provide liquidity for exporters who sold goods and / or services on credit and who will recover from the importer the export value after a maturity of up to one year. Usually, in order to finance the current activity, foreign trade companies resort to revolving loans based on a limit approved by the bank, after a financial analysis of the company. These loans are renewable by mutual consent and are commonly used in order to cover the period between the delivery / supply time and the collection of claims, when the company must meet various current obligations. The current activity of a company refers to the supply-production-sale cycle, and its financing is usually achieved through global working loans and through credit lines.

During the loan period, banks may require contracting companies some financial accounting information on which to perform analyzes that may change the threshold value, as well as certain contractual clauses.

2. Financing approaches concerning financing through global working loans

In the banking practice, **global operation loans** are known as „working capital loans”[5]. This type of loan is suitable for economic operators that guarantee and prove a profitable activity both internal and for exporting. Lending is done in lei and aims to cover costs of stock supply and services necessary for the operation process which ensures firm agreements, both internal and external.

The technical tool based on which it is established the volume of working capital loans is the cash flow containing the proceeds and payments estimated for a certain period of time. The basis of the preparation of the cash flow is the balance sheet, profit and loss account and other periodic accounting reports to be processed in order to obtain the elements and information falling into the principles of analysis of the bank.

Cash-flow is made taking into consideration the following elements:[2]

- the totality of the revenue that will be collected and the payments that will be made in that period;
- proceeds and payments are taken into account for the period in which it is clear that they will actually be received or paid;
- the value of any forecast is determined by the reality of the assumptions presented;
- the availability of liquidity resulted based on cash-flow changes with the proceeds and payments associated with the activities credited in other forms.

In order to establish the cash needs through the cash-flow method we will take into account, on one hand, cash inflows from operating activities, from sales of fixed assets and capital increases or the increased financial and trade liabilities and on the other hand, the liquidity outflows consisting of purchases of fixed assets and current assets, from the reimbursement of debt and losses from operations. Therefore, it can be said that the use of cash flow method to establish the demand of liquidity has the advantage that it covers the entire company activity (operational, financial and extraordinary).

The period for granting a loan for the working capital is usually 180 days, but it can be extended to 12 months since the granting of the first loan installment. If, during the loan period significant differences occur between the level of the indicators established by forecasting at the level of the cash flow and those actually resulted from the regular accounting statements, cash availability can be updated.

3. Financial accounting approaches of financing by currency revolving credit

As mentioned, the financing of companies' current business is often made through short and medium term loans, also known as working capital loans. In this regard, in addition to global working loans, banks make available to foreign trade companies, and not only to them, loans under the form of **revolving loan**. Revolving loan is a loan method based on a loan agreement concluded between the bank and the company. This agreement obliges the bank to make funds available to the company for a certain period of time established by the contract and which can be renewed. Funds requested by calling the credit line are used by the companies in order to cover certain operating needs such as raw materials and consumables stocks, merchandise and other expenses of the current period.

The main feature of a revolving loan is that limited funding is attached to the company current account, and repayments are made after the company receives various claims through the current account.

We believe that, often, foreign trade companies resort to loans for current activity in order to improve the company liquidity, hence a better ability to negotiate with prospective suppliers. Thus, the negotiation of a future business can lead to the establishment of better prices as long as immediate payment is ensured.

In the specialty journalistic field, the credit line is named "rollover loan" because of the way it functions. [7] It is a type of loan which is usually granted for a period of 365 days, but it can also be granted for lower terms of 90 or 180 days. After the expiry of the contractual period, the credit line may be extended if the company has a stable financial situation, without the bank requiring a justification of the use of the financing.

In order to determine the loan amount, banks follow the turnover of the applicant company and the average collection of its customers, reason for which the main elements required are set of annual financial statements for the previously ended year and the related trial balance.

According to authors Ilie Mihai and Tiberiu-Ionuț Mihai *"it is important to note that, in terms of financing the export activity, in the evaluation of the credit line, the calculation will take into account the turnover of exports (usually expressed in equivalent USD or EUR), what percentage of it was rolled by the financing bank, and the average duration of collection of foreign customers related to this activity"*. [2]

For this reason, we consider that the analysis of turnover from export activities could not be performed solely on the basis of annual financial statements and trial balance, because national accounting regulations do not require a separation of internal and external financial statements. Thus, banks are forced to require additional statements concerning export activities of the applicant companies, such as the statement of claims against foreign customers.

The specificity of the credit line is given by the operation mode thereof, which is made base on the revolving system, which is during the entire validity of the line one can make drawings and repayments, provided that the daily balance of commitments does not exceed the maximum level negotiated with the bank by the operator.

Therefore, we can emphasize that the *main advantage of the credit line* is the capacity of financing the proceeds deficit resulting from the existence of a maturity period to suppliers shorter than the maturity period offered to customers. *Another advantage* of the credit line is the fact that interest is charged only for the amount used daily, and in some cases when the amounts remain unusable no fees are charged. The use of credit lines to finance current activities can help maximize profits, as payments are made on time and thus avoid late payment penalties and the company may even receive financial discounts from suppliers for payments made before maturity.

It should be noted, however, that the credit line can have a number of *disadvantages* for companies, meaning that if the amount of the credit line does not meet the real needs of financing, the company's balance sheet can become unbalanced. On the other hand, even if the interest is calculated and deducted only for the amounts actually used, it must be taken into consideration before taking the decision to recur to financing, the additional costs consisting of various fees imposed by the bank (granting, drawing, management).

Also, very important for the applicant company is late payment or credit overruns that can result in the levying of penalties or even cancellation of the credit line.

Looking from the perspective of transactions carried out by a foreign trade company, we appreciate that credit lines requested by such a company can be granted in RON or foreign currency, depending on its option and needs.

Regarding the accounting recording of the transactions generated by the use of a credit line by a foreign trade company, national accounting regulations provide that for the receipt, use and repayment of the loan to use

accounts in Class 5 of the General Chart of Accounts. [3] The methodological norms for account use provide that any interests, fees, penalties be registered through the expense accounts in class 6. In the case of the currency credit line there may occur differences with the accounting record of operations arising from the use of the line, any foreign exchange losses or income that will be recorded, or financial expenses.

Economic-financial transactions characteristic to a credit line imply that the money transfer be made concurrently with the actual transaction. The following steps will be presented in the accounting records:

- obtaining the credit line;
- the use of the credit line in order to pay the overdue invoices;
- any receipts from customers;
- repayment of credit line with interest on the amount reimbursed;
- recording of any exchange differences;
- revaluation of the balance of the currency credit line by the end of the month, etc.

To illustrate how the recording is made for a foreign currency credit line we will follow the case of a Romanian company whose object is allocation of human resources abroad.

On 07.06.2013 the company S.C. SOLUTIONS S.R.L. obtains from the bank a currency credit line for a period of 1 year, with a value of 300,000 Euros, to ensure cash for the current activity with foreign countries. In the accounting records, the steps, during the month of June 2013, are as follows:

1. Recording of the receipt of the credit line attached to the Company current account at the rate of 4,5224 lei/€ Euros communicated by BNR on 07.06.2013:

5124	=	5191*	1,356,720 lei
„Cash at bank in foreign currencies”		„Short term bank loans”/ credit line	

* We recommend using a separate analytical account for highlighting a clear situation of the currency credit line.

2. On 06.13.2013 the company uses the credit line with the purpose of paying overdue invoices totaling EUR 20,000 to the supplier Carler SARL at a rate of 4.4830 lei / €. Please note that the debt was previously recorded at a rate of 4.4090 lei / €, and hence on the date of payment the company will record an unfavorable exchange difference of € 20,000 x (4.4090-4.4830) = -1,480 lei.

%	=	5124	89,660 lei
401 01		„Cash at bank in foreign currencies”	88,180 lei
„Suppliers - foreign”			
665			
„Foreign exchange losses”			1,480 lei

3. On 19.06.2013 the company receives from the foreign customer Doux SARL the outstanding amount of € 45,000, at a rate of 4.4992 lei / €. The claim was recorded at the rate of 4.3072 lei / €, which is why the company will record a favorable exchange difference of € 45,000 x (4.4992-4.3072) = 8,640 lei

5124	=	%	202,464 lei
„Cash at bank in foreign currencies”		4111 01	193,824 lei
		„Customers - foreign”	
		765	
		„Foreign exchange gains”	8,640 lei

4. On 25.06.2013 the company pays per diem to the employees placed abroad the amount of € 98,000 at a rate of 4.4870 lei/€.

625	=	5124	439,726 lei
„Travel expenses”		„Cash at bank in foreign currencies”	

5. On 06.06.2013 the company is negotiating with the bank an exchange rate of 4.4161 USD / € in order to make an exchange from the current account in EUR to the USD account in the amount of € 20,000.

581	=	5124	88,322 lei
„Internal transfers”		„Cash at bank in foreign currencies”	

and

5121 „Cash at bank in lei”	=	581 „Internal transfers”	88,322 lei
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6. On 28.06.2013 (a rate of 4.4588 lei/€) the used credit line is reimbursed, as well as the related interest, taking into account the arising foreign exchange differences.

The used credit line: 207,000€

The interest calculated by the bank: 6,922 lei

Unfavorable exchange difference: 11.582,40 lei

5191* „Short term bank loans”/credit line	=	5124 „Cash at bank in foreign currencies”	922,971.6 lei
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666 „ Interest expense”	=	5124 „Cash at bank in foreign currencies”	6,922 lei
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and

665 „Foreign exchange losses”	=	5124 „Cash at bank in foreign currencies”	11,582.40 lei
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7. At the end of the month the currency credit line balance is revalued at NBR rate of 4.4588 lei / €, hence a positive difference due to lower rate: $(93,000€ \times 4.4588) - 433,748.40 \text{ lei} = 19,080 \text{ lei}$

5191* „Short term bank loans”/ credit line	=	765 „ Foreign exchange gains”	19,080 lei
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4. Conclusions

As a result of all the ideas presented, we consider necessary to emphasize that the line of credit is a banking product increasingly used by companies to finance foreign trade current activity, increasing in countries with a developed economy. Companies choose this form of financing because of the generated benefits of this banking product, of which we can synthesize:

- the determining of the amount of the credit line is achieved by relatively simple technical means, allowing the revision in the sense of increasing or decreasing at any time;
- it works by the revolving system that allows drawings and repayments at any time;
- the granting of the loan may be extended whenever necessary, only if previous operations were characterized by frequency and financial stability;
- the cost of borrowing (interest) is calculated and paid only for the net balance of the loan, as determined by the difference between the amounts actually used and the amounts reimbursed.

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- [5]*** Regulation no. 16 of 12th of December 2012, published in the Official Gazette, Part I 865 20th of December

2012, entered into force on 20th of December 2012 on classification of loans and investments, as well as the determining and use of prudential value adjustments, section 1 .

[6]*** Accounting Law no.82/1991 republished and updated.

[7]*** <http://olteniabusiness.ro/226/dilema-firmei-credit-la-termen-sau-linie-de-credit/>, accessed on 20.08.2014.

[8]*** www.financiarul.ro