

FAIR VALUE IN FINANCIAL REPORTS- IMPACT OF VALUATION AND REVALUATION A CASE STUDY

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Abstract

In order to highlight the relationship between the relevant valuation, the preparation of financial reports that reflect reality and the influence on decisions is based on the main objective pursued by the preparation of financial reports, that reflecting the true picture; the true picture can only be achieved under the conditions in which the elements of the entity are subjected to a relevant valuation process, respectively revaluation. Based on these reports, different categories of users make various decisions with impact, both at a microeconomic and macroeconomic level.

The true picture of the financial position and performance achieved with fair value of all patrimonial elements allows investors to assess risk and decide on investment opportunities, as well as raising capital, the entity's managers can carry out strategic planning and set realistic and sustainable goals, creditors can determine the entity's ability to honor its obligations, increases the confidence of employees and business partners. Correct reporting ensures compliance with financial and tax regulations, preventing penalties or reputational losses.

Keywords: valuation, revaluation, financial reporting, true and fair value

J.E.L. classification: M40, M41

1. Introduction

In an economic environment characterized by dynamism and uncertainty, financial reporting must faithfully reflect the equity situation and performance of entities, providing external and internal users with a solid basis for decision-making. This can only be achieved through an evaluation, respectively re-evaluation of the passionate elements.

The valuation and revaluation of assets are essential processes in modern accounting, having a direct impact on the quality of the information presented in the financial reports. In a broad sense, valuation is an analysis, opinion or conclusion regarding the nature, quality, value or usefulness of certain interests or aspects of a particular property, expressed by an impartial person, specialized in the analysis and valuation of properties. In a narrow sense, valuation is the process of estimating a type of value, for a certain property, on a certain date and materialized in the valuation report. (Anghel et al., 2010). Valuation is a form of quantification by which the accounting method determines the size of the elements of wealth in natural expression and expresses this quantity with the help of the monetary standard. In this way, through valuation, all assets, debts and equity are homogenized, expressed in the same standard and can be centralized. (Todea, 2009)

Revaluation plays an important role in adjusting book values to current market conditions, supporting the alignment of reporting with the requirements of international accounting standards.

Among the factors that produce distortions in the value of patrimonial elements and that make it necessary to evaluate and revalue them, we can mention free prices, the exchange rate of the national currency, the internal management of economic agents (Păvăloaia et al., 2006).

In the evaluation process, a significant influence is given by the evaluator's ability to manage the situations and difficulties encountered. This is only possible if appropriate professional and ethical reasoning is exercised.

The valuation or revaluation significantly influences the structure of the balance sheet, the reported revenues and expenses, as well as the financial indicators of the entity, on the basis of which the different categories of internal and external users base their decisions. Therefore, the choice of valuation and revaluation method is crucial, as it affects the relevance, comparability and transparency of financial reports.

Conceived and structured on a complex issue, this scientific approach aims to present the importance of valuation and re-evaluation in the preparation of financial reports that reflect the true image of the entity and on the basis of which correct and timely decisions can be founded.

2. Methodology

Any research that is intended to be scientific should have a purpose. The purpose of this research is to present theoretical and practical aspects related to the importance of valuation and revaluation in reflecting the real situation of an entity's assets.

The methodology we used in order to carry out this scientific approach is based on theoretical research on the concepts of evaluation, reevaluation, true image, accompanied by empirical research through which we highlighted particular aspects related to the approached concepts. We have resorted to studying the works in the field of financial accounting developed by specialists and theorists in the field, studying the Valuation Standards, analyzing the regulations in the field, being a qualitative exploratory research.

In our research, in order to show the importance of valuation in the decision-making process, we made a comparison of the information reflected by the financial reports whether or not entities carry out a relevant valuation. The arguments that justify the use of comparison consist in the fact that they allow the identification of similarities, but also of the dissimilarities existing between the two types of information reflected by the financial reports.

The qualitative study shall be completed by means of a SWOT analysis of the performance of a relevant valuation of the assets and liabilities contained in the financial reports, with the aim of establishing the strengths, weaknesses, opportunities and threats regarding the provision of additional information by performing or not carrying out the relevant valuation for the preparation of the financial reports, used in the decision-making process by the various categories of users.

For the realization of this study, techniques and procedures will be used, such as: collection and processing of information, creation of various tables, in order to synthesize and highlight the result of the research.

3. General framework of annual financial reports

Through accounting, as a business language, information is processed, in the form of summaries, i.e. accounting documents bearing various names, in order to be used by the various categories of users in the decision-making process. Each synthesis materialized in a certain document, a certain financial report, has an importance, a role, respectively certain functions that it must fulfill, in order to ensure the main objective of accounting.

The annual financial reports or annual financial statements, as they are called in the Regulations according to OMFP 1802/2014, are official documents presenting the economic and financial situation, which must provide a true and fair view of the entity's assets, debts, financial position, profit or loss. (Crețoiu and Bucur, 2007)

Starting from the definition of the financial reports, respectively of the financial statements, we can say that the main objective is to reflect the true image of the entity, in order to allow all categories of interested users to make the most correct decisions.

Information relating to the entity's economic resources shall be useful to anticipate the entity's ability to generate cash or cash equivalents in the future. The information on the financial structure can be used to anticipate future lending needs and how future profits and cash flows will be distributed among those who have an interest in the entity, its usefulness also lies in the possibility of anticipating the entity's chances of receiving financing in the future. The ability to honour the financial commitments due is evidenced by the information on liquidity and solvency (Crețoiu and Bucur, 2007).

The usefulness of financial reports is given by the fact that they present the entity's situation, they represent a means of management. Starting from the information presented in them, specific economic and financial analyses can be made, depending on the information needs of each category of users, performance indicators can be determined, risks can be determined and, last but not least, the value of the entity. By correlating the information provided by the financial statements with other financial or non-financial information from the external environment, a solid decision-making basis is obtained.

Based on the economic and financial reports, the economic analysis allows to highlight the existing difficulties. Thus, it will be possible to calculate indicators, whose veracity and relevance depend on the way in which the evaluation of the structural elements included in their calculation was carried out. These, in turn, influence the decisions subsequently made by the different categories of users. (Gagoare and Vasilescu, 2011)

Obtaining a true and fair view is achievable only under the conditions of compliance with accounting principles, which mainly refer to the constitution and valuation of the items included in the financial statements, on the one hand, and on the other hand, the true and fair view is ensured if accounting policies are chosen and applied so that the financial statements comply with the requirements of all International Accounting Standards .Accounting. Also, the presentation of information is done in a manner that ensures relevance, credibility, comparability and intelligibility, and if necessary additional information must be presented, in order to allow users to understand the meaning of events and transactions. (Todea, 2004)

At the same time, these financial reports can only reflect the true picture if an adequate evaluation is carried out, in compliance with all the standards and current regulations.

4. Theoretical aspects regarding valuation

From a theoretical point of view, we can say that evaluation is, like accounting, a combination of science, art and experience, and depending on when it is performed, it is represented by fair value, market value, replacement cost, use value, acquisition cost, and production cost.

From a methodological point of view, evaluation is an instrument of the accounting method, a complex process, which involves going through several stages, respectively sub-stages, such as diagnostic analysis, application of valuation methods, in order to establish a value of various patrimonial elements.

From an economic point of view, valuation is considered the value assessment of a good, a service, a service or an enterprise in its entirety. When we talk about the valuation of an enterprise, a good or an asset, we can define valuation as a set of techniques, methods and procedures used by the appraiser, through which the enterprise, good or asset in question expresses itself in value at the level of their utility value, respectively of their economic utility. (Todea, 2004)

Valuation is of great interest to the economic environment due to the fact that a large part of operations and transactions cannot be carried out without a proper valuation, decisions having no basis. Among these operations and transactions we mention: placing shares on the financial market,

calculating various taxes and duties, selling the entity, merger-division operations, preparing financial statements.

Relevant valuation has always played the leading role in obtaining financial reports that reflect the true and fair view of the entity and that provide a well-founded basis for the various categories of users in decision-making. However, there are entities and situations in which this is not done and as a result, this scientific approach follows the effects of the financial information contained in the financial reports prepared without an adequate valuation of assets and liabilities and those prepared following the proper valuation of assets and liabilities on decisions.

5. Case study on the impact of evaluation in achieving the fair and true value from annual financial reports

In order to highlight the relationship between the relevant valuation – the preparation of financial reports that reflect reality – the influence on decisions, we will analyze different structures in the balance sheet, by means of a comparison of their value in the situation in which a pertinent valuation is carried out or not, we determine in which elements the greatest changes occur, as well as their influence on the decisions taken by the various categories of users.

The entity considered as an example and which is the subject of our case study is part of the food industry, having as its object of activity the production of meat and meat preparations. Being an entity with the object of activity production, a significant share is represented by tangible fixed assets and current assets.

In the following table we have made a presentation of the situation of the various patrimonial elements, both before the valuation and after the valuation and the revaluation respectively.

Table no.1 Situation of assets

Crt No.	Inv. No.	Name	Value before revaluation	Fair Value	Revaluation difference	
					Reduction	Increase
1.	206	Complex Industrial Meat Processing	1.598.740	1.710.100		111.360
2.	264	Building Wastewater Treatment Plant	87.456	75.834	11.622	
3.	756	Chopping-mixing plant	192.005	186.324	5.681	
4.	-	Commodities	1.780.112	1.792.855		12.743
5.	-	Cash availability	1.833.459	1.833.459		
6.	-	Trade payables	3.391.217	3.391.217		
7.	-	Debts to long-term credit institutions	2.743.566	2.743.566		
Total			11.626.555	11.733.355	17.303	124.103

Source: Own processing

Based on table no. 1, we find that the fair value determined as a result of the revaluation is higher than the value of the items before the revaluation. In the case of certain elements, increases in the amount of 124.103 lei were found, which to a certain extent are due to the modernizations undergone. Reductions in the amount of 17.303 lei were also found.

Until the advent of the GEV 500 valuation standard, the revaluation of buildings had a fiscal impact on the entity because these were the elements for which tax was due, and the tax depended on the value at which the buildings were recorded in the accounts. Also, the tax impact depended on the method of recording in the accounting of the revaluation reserves, by using the net method,

the value of the constructions and buildings that are taxed is lower than the one taxed following the gross method. In the case of the entity presented, the net method is used, being more advantageous.

The appearance of the Gev 500 Valuation Standard developed by ANEVAR which provides for the method of determining the taxable value of buildings and the changes brought by the new tax code regarding what the taxable value of buildings means, thus, if according to the old Fiscal Code the taxable value was represented by the book value, respectively the cost of acquisition, construction, Market value In case of revaluation, currently the taxable value is the value as of December 31 of the year prior to the year for which the tax is due.

The analyzed entity complies with these changes brought by the law of the new Fiscal Code and by GEV 500 and will use authorized appraisers, thus obtaining valuation reports based on which it will be able to pay the correct amount of tax, without being recognized in the balance sheet and without having any influence on the use of the net or gross method.

Considering the value of the buildings, as being also the taxable value, we find that due to the increase in value that was found following the revaluation, the entity will calculate and owe a higher tax.

The industrial meat processing complex represents the center of the entity's activity, being the investment that allows the fulfillment, in optimal conditions, of the object of activity.

The initial valuation of the industrial meat processing complex was carried out at the acquisition cost. Subsequent expenses related to the complex are recognised as expenses during the period in which they were incurred if they are considered repairs or their purpose is to ensure normal use or are recognised as a component of the complex if the conditions for being recognised as investments are met.

At the balance sheet date, the complex is presented at the revalued value. In years in which no revaluation is carried out, it is presented on the balance sheet at the value established at the last revaluation minus the accumulated depreciation.

The depreciation regime used within the entity is the linear one, and the depreciation period is the one provided by the fixed assets catalog, respectively 35 years, (28-42 years).

The value of the complex before the revaluation is 1.598.740 lei. By calling an authorized appraiser, the complex is revalued at 1.710.100 lei. The valuation method used is the cost method, by which the appraiser calculated the cost of rebuilding the complex, taking into account all the depreciations related to it.

Comparing the value established following the revaluation with the initial value, we find the existence of an increase in value by 111.360 lei. With respect to the revaluation reserve, the entity shall use the net method.

The information conveyed by the value of the industrial meat processing complex is useful to various categories of users, such as from shareholders who know the real value of the owned complex and can make the decision to sell or not, respectively to modernize the complex, to the state that is interested in the taxes related to the complex that are due to it.

The building of the wastewater treatment plant has the role of protecting and ensuring the proper functioning of the wastewater treatment plant, so that the content of the water discharged into the environment complies with the limits provided by the regulations, avoiding pollution.

The building was adapted and modernized during the development of the entity's production capacity and implicitly the increase in the volume of water, which required the modernization of the treatment plant.

The initial valuation of the wastewater treatment plant building was carried out at the cost of production. Related subsequent expenditure shall be recognised as expenditure during the period in which it was incurred if it is considered to be a repair or its purpose is to ensure normal use or is recognised as a component of the building if the conditions for recognition as investment are met.

At the balance sheet date, the building is presented at the revalued value. In years when no revaluation is carried out, it is presented on the balance sheet at the value set at the last revaluation minus the accumulated depreciation.

The depreciation regime used within the entity is the linear one, and the depreciation period is the one provided by the fixed assets catalog, respectively 25 years, (24-36 years).

The value of the building before the revaluation is 87.456 lei. Following the revaluation by the cost evaluation method, the appraiser established that its value is 75.834 lei.

Comparing the value established following the revaluation with the initial value, we find the existence of a reduction in value by 11.622 lei.

The mincing-mixing plant entered the entity through acquisition, being initially valued at the acquisition cost, the depreciation regime being the linear one, and the lifespan according to the fixed assets catalog is 14 years (8-14 years). During its lifetime, it underwent modernizations, which were recognized as investments worth 79.137 lei. These modernizations were necessary due to the increase in the entity's production capacity.

The value of the installation before the revaluation is 192.005 lei. Following the revaluation, it is found that the fixed assets suffered a reduction in value by 5.681 lei, thus reaching a fair value of 186.324 lei. The valuation method is the one by market comparison.

The information transmitted by the value of the mincing-mixing line is useful to various categories of users, thus, shareholders who know the real value of the plant can make the decision whether or not to sell the plant, to modernize it, to take it out of service or to change the depreciation regime in the event that they find that it has suffered a degressive depreciation. Managers can determine to what extent using the shredding-mixing line allows to obtain a certain level of product quality, a certain volume of activity, respectively to obtain a certain level of profitability in order to justify the investments made. The public is interested in the plants and machines that the entity uses from the perspective of the quality-price ratio, anti-pollution policies, so there is a justification for the price increase if the equipment used for production pollutes minimally, respectively the quality of the products increases through the use of new technologies.

Due to the fact that the entity has production as its object of activity, a significant share in its balance sheet is held by current assets, which have a decisive role in the smooth running of the entity's activity, which is why the correct valuation of these items is essential in reflecting a true and fair view through the financial statements, so that users can have a solid basis in decision-making.

The goods, they are valued at the cost of the day. On the occasion of the revaluation, there was an increase in their value by 12.743 lei, thus reaching the fair value of 1.792.855 lei.

An important place within current assets is held by **money** available in lei. The value of bank accounts in lei is 1.833.459 lei. They do not support updates, according to the evaluation rules.

Based on this information, shareholders and managers can decide whether they have enough resources for new acquisitions, modernizations, investments, employees are sure to receive the rights they are entitled to, and suppliers are sure that their debts will be paid.

The debts, within the entity, are divided into two categories that have a significant value, therefore a significant influence, namely commercial debts in the amount of 3.391.217 lei, debts to credit institutions in the amount of 2.743.566 lei long-term debts, respectively 385.297 lei short-term ones. These debts are considered to be precisely determinable, being valued at the amount of money necessary to pay the existing obligations. As for bank obligations, they are valued at the balance sheet value, due to the fact that there is no clause in the contract, according to which the appraiser must take into account the evolution of interest rates.

It is important for users of financial reports to know the entity's debt situation in order to have an accurate picture of the entity's ability to finance itself, about the sources of financing and at the same time by correlating the data on liabilities with various other data such as the value of

equity, the entity's profit, the value of receivables, they can calculate and interpret various indicators such as the debt ratio indicator, return on capital, various rotation speeds. These indicators highlight the entity's ability to cover its borrowed capital from equity, the efficiency in debt collection, the entity's ability to pay its interest expenses.

In order to highlight the usefulness of the valuation in providing additional information in the financial reports, used in the decision-making process by the various categories of users, we considered it appropriate to carry out a SWOT analysis, presented in table no. 2.

Table no. 2. SWOT analysis of carrying out a relevant assessment

Strengths	Weaknesses
- More reliable financial reports are obtained, reflecting the true image of the entity - Allows for better comparability in both time and space of the information reflected in financial reports - Improves managers' control over the entity's patrimony - Know the subdomains that present the most common threats to the true picture - It allows the fair valuation of each activity for taxation purposes - Allows the calculation of economic and financial indicators that are based on real information - Allows for better guidance in establishing clauses in contracts with third parties - Improves the speed of reaction of decision-makers by reducing the time needed to obtain certain information	- Requires the provision of the assessment service by an expert - Requires technical and financial resources - In certain situations, there may be situations where there is insufficient staffing - Lack of cooperation between the beneficiary of the assessment and the one providing this service
Opportunities	Threats
- Identification of good practices at national level - Use of various creative accounting techniques specific to revaluation (recording of revaluation reserves, depreciation treatment) - Obtaining a solid foundation in the decision-making process - Allows major transactions: mergers, acquisitions, sales, share issues - Increasing the motivation of the entity's staff, benefiting from real information in decision-making	- Ambiguous, sometimes confusing legislative framework - The existence of large differences between the provisions of the ANEVAR Valuation Standards and the accounting provisions in force - Limits on access to obtaining the necessary information - Exercising inadequate accounting reasoning in carrying out the valuation process

Source: Own processing

6. Conclusions

The main purpose of producing, transmitting and interpreting accounting information, and not only, is its use in decision-making. Decisions are influenced by information both qualitatively and quantitatively, and there is a direct, transparent relationship between the decision and the information, and uncertainty is reduced through information.

The relevant valuation, regardless of the purpose, provides the information necessary for the preparation of financial reports that reflects the true and fair view of the entity. Each element recognized in the financial reports has a series of particularities in terms of valuation and revaluation, respectively, particularities that the valuer must take into account when establishing the values attached to these elements in the reports. These particularities may refer to the valuation bases, the values at which certain assets can be assessed, respectively to the valuation methods by which certain elements can be assessed. Even if expert evaluators encounter various threats, represented in particular by the legislative framework, they, by using appropriate professional judgment and taking into account known good practices, can carry out a relevant evaluation.

The usefulness of financial reports is given by the fact that they render the entity's situation, represent a means of management, allow economic and financial analysis, determination of performance indicators, risks and last but not least the value of the entity.

Based on these reports, the various categories of users can benefit from a solid basis in decision-making. Managers and shareholders need valuation to know the real profitability of the entity. Investors are interested in investing their capital in profitable businesses, the employed staff is interested in the economic and financial stability, the creditors are interested in the market value of the entity, in order to repay loans and pay interest, the state is interested in the valuation process for various purposes, from tax purposes, to expropriation, privatization, etc.

Asset valuation and revaluation are essential tools for increasing the accuracy, transparency and usefulness of financial information. Done correctly, they contribute to a better understanding of the entity's economic situation and support informed decision-making by users of financial reports.

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