

Theories and Methods of Assessment that have Influenced International Practices

Cristina Mihaela ONICA

cristina_onica@yahoo.com

Dunarea de Jos University, Galati, Romania

Lucian DOMNITEANU

lucian_domnitanu@yahoo.com

Abstract. While some theorists have been reluctant to express their opinions and give solutions to the problem of evaluation, in addition to other issues earlier review, sought in the theories developed to propose various methods for assessing balance sheet structures. Retrospective evaluation systems adopted in the theories developed in balance over time results in finding that "some theorists have resorted to an evaluation price of all elements in balance, while others, to ensure a higher accuracy of assessment operations, have adopted several different prices "for various structures of the balance sheet.

Keywords: evaluation, methods, price, market

JEL Code: M19, R32

1. Introduction

While some theorists have been reluctant to express their opinions and give solutions to the problem of evaluation, in addition to other issues previously examined, have sought in the theories developed to propose various methods for assessing balance sheet structures. Retrospective evaluation systems adopted in the theories developed in balance over time results in finding that "some theorists have resorted to a single price of all elements evaluation in balance, while others, to ensure more accurate operations assessment, have adopted several different prices"[1] for various structures of the balance sheet.

2. Theories with a single price value

Some theorists, such as H. Nicklisch Walter le Coutre, Fritz Schmidt, H. Sommerfeld, Wilhelm Rieger in theories developed and addressed the problem of assessment balances structure proposed for choosing evaluation methods based on single question:

- method of purchasing price (purchase);
- replacement value method or the day price in moment of closing the balance-sheet;
- method of valuation at the lowest price possible;
- liquidation price method

a.1. Method of purchase price (purchase) proposed by a representative of monistic theory and a representative of the dualist theory has been improved along the way depending on the economic growth and development of science. Prof. Dr. H. Nicklisch, proposes *in static theory* of balance an assessment of structures to balance price the day balance, when procuring goods combating assessment over the purchase price or cost effective. Regarding

depreciation they proposes, amortization directly to the waiver which is replaced by indirect redemption, by using the "buffer fund", which corrected, in fact, as the book value of purchasing fixed assets. Such evaluation purposes to satisfy static balance sheet to present evidence and make capital goods and the company at a time, which can be compared with the balance of previous results, will be determined through the profit and loss.

Walter le Coutre (Totale Bilanz, Stuttgart-1956) in *the unitary theory, full or total balance sheet, developed in fact static theory*, tier, attributing the balance sheet to present the company assets and that of the benefits or losses. In terms of assessment, Walter le Coutre evaluates all claims to the purchase price, considering the indirect decrease (accounting) depreciation of binding. It is prudent assessment advocates in the sense that do not accept many reservations or occult ones, although he accepts the laws.

a.2. Method of replacement value or the price day in the moment of closing the balance-sheet, supported by Prof. F. Schmidt (Die Organische Tageswertbilanz -1921) from the idea of maintaining the operation of the company as an economic and under inflation influence of the years 1920-1924 concludes the necessity of assessing the prices which take into account different conjunctures. F. Schmidt is based on the thesis of Adam Smith, who considers a man as rich or poor according to the means available in order to procure the necessary goods. He considers that, differences in benefit assessment are not making distinction between the benefits of increases in sales and property due to changes in value. Assets of the people or company are not staying in money, but in goods. According to this theory the benefit is not the difference between production cost and selling price, but the difference between selling price and cost of production calculated, but, not by the supply price, but depending on the prices replenishment which, possibly, between times, have changed due to differences conjunctures occurred.

a.3. The assessment of the possible lowest price method supported by H. Sommerfeld (Eudynamiche Bilanzlehre-1936) considers that the assessment of the lowest economic value (so considering all internal factors that could affect over it) ensure the existence of the company regardless risks that might occur in its the activity. In this theory are found germs of today's circumspection principle.

a.4. Liquidation price method supported by Wilhelm Rieger, in the realistic theory (nominalist)of balance sheet (Introduction to the private economy - 1928), considers only real review the one perfected on base of an assessment in case of company liquidation . The remaining balances, respectively the periodicals, including annual, are considered fiction made only for control purposes, based on assessments by roughly so unreal.

3. Theories with more value prices

Other theorists such as E. Schmalenbach in the two monist theory developed and Gino Zappa, Theo Limpberg, Ernst Walb in dualist theories proposed, have supported the use of several kinds of prices for the assessment of the different characteristics of balance sheet items. Among the theories that have adopted assessment systems with several kinds of prices we can mention:

b.1. Dynamic Theory developed by Prof. E. Schmalenbach (Dynamische Bilanz - 1916) subordinate the evaluation purpose assigned to the balance sheet, and a tool of analysis for determining the causes which led to the company results. It argues the need for setting standards of evaluation for each item patrimony, which will allow stating the results in their entirety, results comparable with previous years. It also, stresses the need of delimitation of the period costs of previous ones due to future periods.

b.2. Gold balance theory, developed by Prof. E. Schmalenbach (Goldmarkbilanz, Leipzig-1922) notify as the effect of inflation in the years 1920-1921 that assesses whether the result of one or more price, is affected by the phenomena of exchange and conjunctures. He adopts the solution of the balance sheet in two values, respective in paper currency and gold. His approach was generated by the need to shelter assets from influences of foreign currencies and conjunctures aroused from the expansion of markets and inflationary event phenomenon.

b.3. Economic theory, developed by the Italian Ginno Zappa and supported by the Belgian Theo Limpberg, considers that the evaluation of assets should be priced for sale, except the means of production for which the assessment should be made at replacement price.

b.4. Economic-financial balance theory, developed by Ernst Walb (Financial Results - 1943), which as stated previously is a development of dynamic balance, focus on existing capital, since it's conception of Walb represent the vital element of the company, balance being used as a tool for monitoring and provision of this capital [2].

Of course and assessment is linked to this end, supporting the assessing procurement of capital value, which, however, applies corrections based on any currency fluctuations. Attempts made by various academics to give complete and acceptable solutions to these difficult problems of assessing the balance sheet items have remained more or less useless. Any price system would take and what would seek balance sheet items assessing the adoption of appropriate pricing for each specific part, the results can not be certain, it is necessary to accept a greater dose or less than relativity. In fact in an article published in the Magazine for economics, Wolfgang Stiltzel proponent of the theory of the balance analysis function identifies three groups of amounts entered in the balance:

- amounts resulting from the simple calculation: the balance of the house, *house turnover*;
- legal operations: capital base, legal reserves, *free reserves*;
- amounts of assets representing objects itself.

On Stiltzel's opinion first two groups may be determined precisely, exactly, but the third group which are determined by the assessment, may be determined exactly only in exceptional cases.

Concerns on the assessment of structures reflected in the balance sheet assets have influenced the time the assessment methods used in international practice. Foreign economists Charpentier M., Hamelin, Leo Chardonnet, G. Snozzi, but also romanians as Jacob Petru Pantea, Ioan Căinap, Liviu Henegar, Ioan Popa approached the assessment methods that have long influenced the accounting states legislation. These may be grouped as follows:

- *old methods of evaluation:*
 - rollback prices method;
 - market price method;
 - the method of liquidation value;
- *assessment methods relatively new:*
 - individual subjective value method;
 - replacement value method.
- *specific methods to certain elements of balance sheet assets:*
 - the method of yield;
 - future course method.

Evaluation of active assets according to *the method of returning pricing* has taken in consideration all expenses made by the company (to take in possession) which decrease the amount of annual redemptions. This is an exceptionable method, whereas subjective assessments can generate the value intakes in nature and arbitrary determination of price of goods manufactured for own needs by the company.

Market price method requires the evaluation of assets at the price of exchange on inventory. So, the price at which assets are valued, the price is set based on supply and demand, which they could be bought on the day inventory. M. Charpentier and Hamelin criticize this method, considering that is "committed a mistake of principle evaluation the current prices of active elements, which have for company a value of service and authorize the distribution of dividends based on a simple finding of increased values". So, the method leads to the distribution of dividends to shareholders, before being actually made. Therefore in practice, on grounds of prudence, the market price and price reversion method were combined evaluating the assets at the lowest price between the two. Also on the grounds of prudence, to avoid distribution of unrealized profits, Bosvienx M. Houpin in "Traite theoretique et pratique des civiles et societe commerciales" offers an intermediate method. It consists in assessing the asset return price, when their value can not be determined exactly according to the price of similar assets and current price. Also, if possible, in a special reserve fund must be registering the price increases to avoid the distribution of dividends prior to their effective implementation.

The liquidation value method takes in consideration the probable price that would be obtained in the event of company liquidation. Introducing a presumption of liquidation, the method generates a subjective and uncertain evaluation [3]. Claiming that the assessment should be made on items subjective and not objective, *the subjective individual value method* states the need of taking into account the owners benefits can or not obtain and not the utility assets for third parties. Therefore, must be taken in consideration the individual value of each item. However, in practice, the subjective value can be confused with the return price and the goods to the market price, supported by some methods outlined above.

In an inflationary economic environment *replacement value method* aims to avoid risks generated by price fluctuations. Valuation of assets at replacement cost has utility, where wear moral means of production which generates considerable reduction in the value and avoid risk of damage to capital by currency instability. Speaking about the method of yield value G. Snozzi shows that it is specific to tangible assets. Where, due to various factors excessive amount of fixed assets generates a too high depreciation, the company may record losses to other similar companies. To eliminate waste it is proposed to determine the value (called the yield in literature) property that ensures normal depreciation and financial reclamation, by supporting additional expenditure from reserves. The *method of achieving future course*, applied only in stocks, is to evaluate stocks for sale at the price of future achievement, expected at the balance sheet date. This requires knowledge of two hard foreseeable with certainty the future price and the likely date of sale. In practice, the method entails, evaluation of finished products and production manufacturing being the selling price forecast less deviations, determined on empirically debates, depending on the stage of finishing products. In conclusion, this method generates subjective assessments. Of those exposed results that theory accounts showed an ongoing interest in determining the direction value of the economic structures of the balance sheet.

Showing the great importance of "coordination of national provisions on the structure and content of annual ..., assessment procedures," Fourth Directive of the European Council considers that the annual ... the need to present an accurate picture of the heritage, financial position and companies results" and "different ways of assessment should be coordinated so as to ensure equivalence and comparability of information contained in the annual accounts. These provisions are entered on the International Financial Reporting Standards which deals in General aspects of "Qualitative characteristics of financial statements" and "Evaluation of financial structures ". On the world level we can see the continuing integration of states world economies, the trend of formation and consolidation of regional economic union and the existence of large companies operating outside the country.

In conditions of economies globalization, of financial markets integration and information systems, users have requested that the information given by the balance sheet, to ensure comparability over time and space between companies located in different points of the planet. In the context appeared an international body represented by the International Accounting Standards Board (IASB) that has proposed and realized the developing of International Accounting Standards, whose targets are:

- development and publication, in public interest accounting standards that will serve as the basis for presentation of financial statements, and promote *global level*, acceptance and compliance with them;
- development of activities in directions to improve and harmonize regulations, of accounting standards and procedures for submission of financial statements.

Their appearance has generated remarkable progress in improving and harmonizing financial reporting worldwide. Accounting harmonization pressure comes both from those who use accounting information (such as investors, financial analysts, banks, third party lenders, stock exchanges and regulatory authorities of the capital market) and from the national standardization and regulation of accounting profession . These advantages are presented for the national governments of states, which can track and control operations of multinational companies and numerous intergovernmental bodies such as the European Communities Council. Evaluation of economic structures in the balance sheet in the European Union and Romania will be addressed through the IAS/IFRS. Regardless of the format used, the assets are valued in principle to the purchase price or cost of returning, however, the possibility exists that the Member States authorize the use in certain situations the amount of replacement and procedures and judgments that take into account the influence of inflation and other factors generating price fluctuation.

Elements of fixed assets are valued at purchase price obtained by adding the purchase price of expenditure accessories, if they have been purchased from third parties. The other products inside the company is valued at the cost of return consists of the purchase price of raw materials and materials, direct labor and indirect costs apportioned on the product. It supports the inclusion in the cost of return of interest for borrowed capital to finance the manufacture of fixed assets, only insofar as they relate to the period of production. Since the elements of fixed assets whose use is limited in time, undergo a physical and moral wear, should aim *value adjustments calculated to systematically v pay off their value during use. These corrections diminish the value of the purchase price or cost of returning.*

Financial fixed assets can be only as long as there are justifiable reasons, subject to value adjustments to give the lower value items to be given to drawing up the balance sheet date. These value corrections have overlooked value in profit or loss and shown separately in the notes [4]. Items assets valued at purchase price or cost of return may be as long as there are justifiable reasons, subject to corrections of value to give these elements a lower value than the market or in special circumstances, another lower value to be attributed to the balance sheet date.

Member States may permit *exceptional value adjustments*, if they are necessary based on a reasonable commercial assessment to ensure that, in the near future, assessment of these elements may not be modified because of fluctuations in value. The total value of these corrections should be shown separately in the profit and loss account or in the notes. *Purchase price or cost of returning stock items in the same category and all fungible items can, if member states support, to include the calculated values, or the "weighted average price" or the methods" first came out-first "or" last-come first out "or a similar method.* If the evaluation yields a difference of significant value on the balance sheet date, through an assessment on the last market price, known before the closing balance sheet value of this difference must be globally, by category, in the notes. *On the grounds of tax items in both fixed assets and the*

current assets may be subject to corrections exceptional value. In the case of debt, if the amount to be refunded exceeds the amount received, the difference may be highlighted separately in the balance sheet asset and depreciated at the latest when the debt repayment.

As regards provisions for risks and outgoings, it must specify that they do not exceed requirements. The explanatory notes have the following detailed information:

- assessment procedures and methods applied for calculating the value adjustments;
- number and nominal value or in the absence of nominal value, the accounting of the shares subscribed during the year in the authorized capital, the detailed categories of actions;
- the beneficiary parties, bonds and convertible securities or similar rights with an indication of their number and scope of coverage of the rights they confer;
- amount of debt of companies which is the residual term of more than five years and the amount of debts covered by the guarantees given by the company, indicating their nature and form;
- total amount of financial commitments which are not included in the balance sheet to the extent that their indication is useful for assessing the financial situation. Commitments which are in matter for pensions and commitments related to companies must be distinct highlighted ;
- allocating the value of net turnover by categories of activity and geographical area;
- average number of employees during the year divided by categories and related with personal expenses budget;
- proportion in which the calculation result of the exercise was affected by an assessment of the economic elements of active and passive, to benefit from tax simultaneously, with its justification;
- difference between fiscal expenditure and tax year and previous years tax expense already paid or payable under these exercises, to the extent that this difference has a clear interest on future tax expense;
- comprehensive information on salaries in the budget allocated for the administration, management or supervision and commitments arising from contracts or pension contracts for former members of these bodies;
- global information on the amount of advances and loans granted to members of the administration bodies, management or monitoring, indicating the interest rate, the amounts repaid and the guarantees made.

4. Conclusions

From the above it follows European states care to harmonize the information provided by European companies' balance sheets so that users can assess the management of the company and can eliminate or at least reduce the risk of uncertainty, which negatively affects the decision making process.

References

1. Florea I., Florea R., Macovei I.C., Berheci M., *Introduction in assessment expertise and financial audit*, CECCAR Publishing House, Bucharest, 2005, p.141
2. Georgescu I., *Applied assessment elements in companies and public institutions*, Sedcom Libris" Publishing House, Iasi, 2005, p. 120
3. Georgescu I., Macovei C., Berheci M., *Company accounting*, "Junimea" Publishing House, Iasi, 2003, p. 85
4. Horomnea E., Berheci I., (cood), *Standardization and harmonization of Romanian accounting*, "Sedcom Libris" Publishing House, Iasi, 2004, p. 78