

RELEVANCE OF FINANCIAL STATEMENTS INFORMATION FROM SMEs PERSPECTIVE

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Abstract: This paper considers the information presented in the financial statement by small and medium sized enterprises (SMEs) and its role in business decisions. In particular, attention is focused on data presented in abridge financial statements and the lack of reliable information in this documents, which comprises a trustworthy financial analysis in case of micro and small business. Financial statements allow internal and external users to draw up conclusions about the financial position and performance of the business, generating information about cash flows, costs, revenues, and profit margins. For external users, financial statements are also the only source of information. In this regard, some of the current limitations of the information presented in the abridge form of financial statements will be detailed in the current paper. Furthermore, recommendation for improving the current situation will be proposed. This paper has been drawn up, using the official statistical data, the legal framework and own reflection of the author.

Keywords: financial statements, SMEs, business decisions.

JEL Classification: G30

INTRODUCTION

A successful business depends on the timely adoption of appropriate managerial decisions. Usually, any managerial decision is based on a mix of internal operational data and external market sources [3]. Among these, data presented in financial statements allow both internal and external users to take the right decisions and to conduct a profitable business.

Currently, in local practice, various categories of entities prepare and present one of the following sets of financial statements: abridged, simplified and complete. Requirements regarding financial reporting and the preparation of Financial Statements are stipulated in the Law of accounting and financial reporting No. 287 from 15/12/2017. According to the Law, the category of micro entities and natural persons that conduct entrepreneurial activity, once registered as value-added tax payers, draw up abridged financial statements according to National Accounting Standards (NAS). Small entities draw up simplified financial statements according to NAS. Medium-sized and large entities draw up complete (full) financial statements according to NAS. In this regard, the entity can be classified in one of the following categories if, at the reporting date, two of the criteria presented in table 1, are respected.

Table 1: Categories of entities form the perspective and requirements of financial reporting

Category of entities	Total value of assets, MDL	Total value of revenues from sales, MDL	The average number of employees, persons
Micro entity	≤ 5 600 000	≤ 11 200 000	≤ 10
Small entity	≤ 63 600 000	≤ 127 200 000	≤ 50
Medium entity	≤ 318 000 000	≤ 636 000 000	≤ 250
Large entity	> 318 000 000	> 636 000 000	> 250

Source: Law of accounting and financial reporting No. 287 from 15/12/2017.

Given the high value of assets and revenues for local market, presented in table 1, the majority of entities will be attributed to the micro business sector, which means that they will prepare and present abridged financial statements. Moreover, analyzing data from financial statements, and especially abridged ones, users often face some limitations in performing an objective and correct analysis of the entity's economic and financial activity. This is primarily due to the limited information available to an analyst when analyzing the financial condition of an economic entity solely based on financial statements, without using any internal accounting data.

In case of small and medium sized enterprises (SMEs) that often face financial gaps, it is crucial to present a detailed information about the business to external users, in order to attract potential investor and to grow up business. In this regard, we will have a close look at some specific limitation that affects in particular SMEs.

RESULTS AND DISCUSSIONS

One of the common limitation is the difficulty to determine what is the main type of activity of the entity (production; sale of goods; provision of services, etc.), and which of these generates the highest amount of revenues from sales. The abridged template of the Profit or Loss Statement, doesn't allow such an analysis, since it reflects only the total amount of revenues from sales, without specifying the main source (from the sale of products, from the sale of goods, from the provision of services, from the execution of works, from construction contracts, from operational and financial leasing contracts (rent/lease) etc.).

Therefore, in order to determine whether, during the management period, the main type of activity (for example, production) is also the one that generates the entity's highest revenues from sales, it is necessary to use additional accounting data and/or the explanatory note. Additional sources may include detailed data from the account "Revenues from sales" or the information from the trial balance of the same account. If it is necessary to examine the revenues from sales recorded on sales markets, the data can be obtained by correlating the information from the account "Revenues from sales" and account "Trade receivables" or the disclosures in the explanatory note.

Furthermore, the decision-making process also concerns the use of the entity's productive potential, technical capacity and the process of renewing fixed assets. For example, when an entity is applying for a bank loan with the propose to renew the fixed assets, financial institutions examine such indicators as the book value of the fixed assets, depreciation of fixed assets during the management period, the value of fixed assets leased, etc. Unfortunately, this kind of information cannot be found in the abridged financial statements or even in the complete one (except for the book value of fixed assets). In this case, financial institutions will request additional accounting information from the account "Fixed assets" and account "Depreciation of fixed assets", and disclosures from the explanatory note on fixed assets.

A major concern within any entity is the collection of receivables and the payment of debts. The increase of both negatively influence the activity of the entity. Therefore, in order to prevent the emergence of doubtful debts and the increase in the entity's dependence on creditors, the entity should constantly analyse the size, evolution, structure and the collection/payment period of receivables and debts. Unfortunately, the financial statements prepared and presented by enterprises in the small business sector, do not include all the information necessary for performing such an analysis.

Abridged and complete financial statements suffer from the lack of information concerning the size of receivables and payables by the date of occurrence and the nature of payment.

Moreover, abridged financial statements do not include any data about the types of long-term and current receivables/payables, receivables from affiliated parties and payables to affiliated parties, advances granted and advances received, which does not allow users to make the right decisions related to the management of receivables and payables. If internal users can obtain such information from the accounts: "Trade receivables", "Corrections (provisions) on doubtful receivables",

"Receivables from affiliated parties", "Current advances granted", "Budget receivables", "Employees receivables"; data from the records of contracts concluded with each client and explanatory note, then external users do not have the opportunity to examine the entity's receivables and liabilities in detail.

The situations described above, confirm that the information presented in the abridged template of the financial statements is insufficient for a detailed assessment of the entity's activity. In order to obtain an adequate assessment of the entity's activity and to take business decisions, it is desirable for entities to use additional accounting data and data disclosed in the explanatory notes.

Another issue concerning the limits of the financial statements, which we would like to highlight in the current paper is the lack of a normative basis for assessing financial indicators. Currently, in the process of analysing financial indicators, such as: liquidity, profitability, solvency, financial stability, the current levels recorded by these indicators are compared with the "recommended norms" or "optimal ranges".

Furthermore, in the local analytical practice, we do not have an official document that would recommend/establish these norms, in the process of analysis, norms or optimal ranges recommended in various bibliographic sources and used by local entities are mostly taken from international experience. For example, in the literature review we can find that the optimal range of current liquidity is between "2-2.5, or 1-2.5 or even > 2 " [2]. So, the question arises: to which of these ranges should the current liquidity level correspond?

The optimal ranges recommended for various financial indicators depend on the field of activity. Therefore, taking in consideration the lack of normative basis for comparison, financial indicators are assessed in dynamics. However, we advise the responsible bodies and ministers to develop a framework with the recommended ranges for various indicators, both financial and non-financial.

In the analysis of financial statements, we also noticed the lack of a single approach in calculating some financial indicators. For example, when calculating the current liquidity indicator, it is necessary to report the value of current assets to current liabilities. If the information is taken from the entity's balance sheet (regardless of whether it is abridged or complete template), the obtained result will not reflect correctly the entity's solvency. The main reason for this is that according to the current balance sheet template, in the composition of inventories (as part of current assets) are also included the amounts of advances granted for long-term and current inventories. In this regard, when we use the total amount of current assets from the balance sheet data, we artificially increase their value with the value of advances granted for long-term inventories. Therefore, when an entity needs to calculate the value of current assets, we recommend to exclude the value of long-term advances granted for inventories, from the total amount of current assets.

On the other hand, in the current template of the balance sheet, both long-term and current provisions are shown as a separate subchapter. In this regard, if for the calculation of current liquidity we use only the total amount of current liabilities, we will also obtain a false result, since the value of current provisions is not taken into account. The issue of including current provisions in the composition of current liabilities when determining liquidity indicators is a discussed one. In the current paper, we consider that the value of current provisions is a component part of current liabilities; therefore, they must be taken into account when calculating various financial indicators, just as long-term provisions must be included in the composition of long-term liabilities.

CONCLUSION

The study conducted in the current paper allowed us to conclude that the lack of data in financial statements, the absence of a normative basis for assessing financial indicators, as well as the lack of a single approach in calculating financial indicators represent the main problems faced by users of financial statements. The results of the financial analysis and the managerial decisions taken depends on the quality and complexity of the information presented in the financial statements.

Currently, the abridged template of financial statements, prepared and presented by most domestic entities, do not contain sufficient information for an objective assessment of the financial

position and financial performance of micro entities. When an entity calculates different financial indicators, it is necessary to take into account the economic meaning of the patrimonial elements, as well as the significance of each indicator.

Furthermore, it would be desirable to have a normative document that would recommend some ranges for different financial indicators, established in accordance with the specific features of the branch and field of activity of the entity. The established and applied ranges do not generally take into account the industry in which the entity operates. For small business, it seems more appropriate to track trends in these indicators dynamically over a number of reporting periods, rather than compare financial performance indicators with accepted standards, due to the specific nature of their operations.

The recommendations offered in the current paper related to the analysis of the financial performance of SMEs based on financial statements data, will increase the objectivity of managerial decisions.

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