

Application of the Evaluating Methods of the Stocks at the Exit from the Patrimony in Romania

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Abstract

In the present paper I intend to approach the evaluation of material current assets at the exit from the heritage, considering the changes occurred in recent years in the accounting system from Romania and considering the importance that the stocks has on the result of the exercise. Throughout the paper we highlighted the general aspects regarding the stocks, stocks evaluation, and also the advantages and disadvantages in the use of evaluation methods of the stocks at the exit from the patrimony from the Romanian system. Starting from the aspects with general character and in full conformity with International Accounting Standards, we presented calculation methods used in evaluation of stocks at the exit from patrimony.

Keywords: CMP, evaluation methods, FIFO, LIFO, stocks.

1. Introduction

We paid a special in this scientific paper to presenting the problem of accounting of goods, of theoretical and practical aspects of it's and evaluation of stocks at the exit from patrimony from Romania.

In the first part of the paper we have defined and classified the stocks according to several criteria's. In the following we listed the main methods of stock evaluation, namely: evaluation at *the entrance in patrimony* through: acquisition cost, production cost, input value and the utility and other costs occasioned by the entered stocks; and *evaluation at the exit from patrimony of the stocks*: the method of specific identification, the method of weighted average cost (CMP), the method first in-first out (FIFO) and the method last in-first out (LIFO) with advantages and disadvantages own of each valuation method.

For the elaborating this work we consulted as source of information and documentation, the reference works of authors from the field, journals, laws adopted by the Ministry of Public Finance from Romania and the International Accounting Standards.

2. The content, structure and stock evaluation

International accounting of stocks is described in detail in "*International Accounting Standard no. 2*" whose main objective is to describe the accounting treatment of stocks in historical cost system, standard that provides information regarding to the recognition of the stocks value of inventories at the date of balance sheet, determination of the cost of stocks and recognition of expenses with stocks, considering any record at the net realizable value and clarifications regarding the practical procedures of determination of stocks costs.

Stocks are assets: [1, 2]

- *Held to be sold during the normal development of activity;*
- *Under production to be sold in future periods;*

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- Under the form of raw materials and consumables, used for the production of some goods or achievement of some services.

Framing the stocks in the category of assets, in terms of their diversity, raise the question of their delimitation by other assets, especially by those that take the material form (the body one). In this respect, are taken into account criteria's that aim specifically their nature of assets and role in the operating activity.

According to the criteria's mentioned above, the stocks are goods or services that transforms into cash availability within a year, being known under the name of current material assets.

The definition of stocks according to the International Accounting Standard no. 2, reveal, directly or indirectly, *three criteria's* according to witch they are classified and defined in financial accounting: physical, the destination, the phase of operating cycle (Figure 1) [3].

<i>Classification criteria</i>		
Physical criteria	By destination	The phase of operating cycle
<ul style="list-style-type: none"> • raw materials, directly involved in production, being found partly or wholly, in their composition; • consumables (fuel, fodder, spare parts) • inventory objects materials; • young animals, animals for fattening, birds and colonies of bees; • packaging (except packages such as inventory objects and tangible assets). 	<ul style="list-style-type: none"> • stocks designed to achieve the objective; • stocks produced by the enterprise designed for sale; • stocks that are in course of execution; 	<ul style="list-style-type: none"> • stocks in the supply stage: of the production activity, of the commercial activity; • stocks in the production stage; • stocks in the marketing stage.

Figure 1. Classification of stocks

Referring to the evaluation of stocks at the level of the accounting system from our country, we can say that, in the condition of the market economy, financial accounting should provide accounting and control of managements of material values, but also ensuring the informational base for costs calculation cost. Also, a significant problem for accounting is the evaluation of stocks, given the effects of liberalization and price negotiation that can lead to changes in their value from one reporting period to another, with pro and against influences on the costs of production and circulation. In general, the evaluation of stocks entries in the heritage, don't raise problems, because all information used, regarding the quantities and prices of those are taken right from supporting documents. The evaluation of stocks exist raise difficulties in practice terms, because they come from different inputs whose prices can vary and the accounting has the task to evaluate the exits, for the final stock to be properly evaluated, so that "any differences of price with conjuncture character must affect the costs of the period to which they relate [4, 5].

3. The evaluation of stocks of the exit from the heritage

The evaluation of stocks and of the production in progress is made at different stages of the development of economic activity, namely: at the entry into heritage; at the exit from the patrimony or switching to consumption; at inventory; at the end of economic-financial exercise [6].

The exit of stocks from management is made, mainly through consumption and through sale. The fundamental problem that arises for recording the exit of stocks is the one of the price used. In this regard, the norm IAS-2 groups the stocks according to their ability to identify themselves in: identifiable stocks and fungible stocks. The evaluation of consumptions/exits of stocks from patrimony has on base their value of entrance and can be done by several *methods of evaluation*:

- For identifiable stocks: the method of identification (IAS);
- For fungible stocks:

A. As basic accounting treatments:

- The method of weighted average cost (CMP);
- The method of "first in - first out" (FIFO);

B. As an alternative accounting treatment:

- The method of "last in-first out" (LIFO);

C. Other treatments (techniques for measuring costs):

- *The method of price fixed (standard cost);*
- *The method of retail price* [7].

Regarding the International Accounting Standard, it describes the methods of applying only to a very general way and any method commonly used is apparently acceptable. But regardless of the method of application used, it should be used in a consequent manner. **International Accounting Standard 1** debates an aspect regarding the possibility of a society to use different methods for calculating the cost for different types of costs. The interpretation provides that "an enterprise should use the same methods of determining the cost for all stocks that have a similar nature and usage for the enterprise". But, for those who have a nature and a different way of usage, is justified the usage of some different methods of calculation [8].

From this perspective, I found the fact that, in the Romanian system there is no prevision if an enterprise must use a single formula for determining the costs for all the stocks that it holds in its distribution network, instead can use different methods for different stocks. So, it confirms that each entity can use any of the following methods such as: the method of weighted average cost, FIFO and LIFO for costs allocation to different classes of stocks, which presents different characteristics in terms of the nature and use of their. For example, the LIFO method can be used for certain types of stocks or production lines, FIFO and the method of weighted average cost for others.

The method used for a certain class of stocks must be used consequent for that class for the activities in the international network and from one period to another. In addition it calls that the same formula of cost determination to be used for all stocks with similar characteristics in terms of nature and the way of use them.

In case of using the LIFO method, it highlights the difference between the balance sheet value of the costs and: either the lesser value between the cost calculated according to FIFO or weighted average cost and the net realizable value, or the lower value between current cost at the balance sheet date and net realizable value.

As we can see, also in this chapter is done after the tax and accounting rules of the International

Accounting Standards regarding to the evaluation of exits of stocks from patrimony. In Romania the evaluation of stocks at the exit from patrimony is realized using, mainly, the three methods: the weighted average cost (CMP), "first in - first out" (FIFO) "last in - first out" (LIFO) [9, 10].

Once selected a valuation method, it must be maintained from year to year. Any change in the coming years is stated and justified in the explanatory notes to the Annual Financial Situations, together with the effects of those changes on the balance sheet and on the economic and financial situation.

4. Advantages and disadvantages in the usage of stocks evaluation methods at the exit from the patrimony from Romanian system

Starting from the methods of stocks evaluation at the exit from patrimony, we have established which are the advantages and disadvantages in their usage at national and international level.

When we speak about *the method of weighted average cost (CMP)*, we must know that it is calculated as ratio between the total value of initial stock plus the value of the entries, on the one hand, and the amount existent in the initial stock plus the amount entered on the other side. This method involves the monthly calculation of average cost or after each, input operation, and the usage of the method requires keeping an operative, quantitatively and value evidence.

In the Romanian system, the method of weighted average cost is calculated according on two criteria's, namely: *the method of weighted average unit cost calculated at the end of the period* (or the method of weighted average unit global or total cost), and *the method of weighted average unit cost calculated after each reception*.

Determining the weighted average cost depending on the two criteria's has advantages and disadvantages (Figure 2) [11, 12].

Referring to the method of "*first in-first out*" (FIFO), according to that method, the stocks exit from management are evaluated at cost of acquisition or production of the first entry or of the first group, and on the extent of group exhaustion, the goods out from management are evaluated at cost of acquisition or production of the next group, in chronological order. At our country level, FIFO method, presents both advantages and disadvantages (Figure 3) [12].

ADVANTAGES	CMP method at the end of the period	<ul style="list-style-type: none"> - To level cost variations (price) in case of the course fluctuations; - To simplify the calculations of stocks evaluation
	CMP unit method after each reception	<ul style="list-style-type: none"> - The value of stock and of the exits from the stock are permanently known; - The value of the exits so calculated outputs are closer to the economic reality from that moment.
DISADVANTAGES	CMP method at the end of the period	- do not allow the evaluation of each exit from the stock, but only their global evaluation at the end of the reporting period, which is in contradiction with the basic principle of the permanent inventory: the ability to determine in any moment the value of the final stock.
	CMP unit method after each reception	- due to its complexity, the usage of this alternative of calculation of weighted average unit cost is difficult especially for operating cycles in which the stocks movements are very numerous

Figure 2. Advantages and disadvantages of the method of weighted average cost

Sources: Iacob, Constanța, Ionescu, I., Avram, Marioara, 2012

ADVANTAGES	<ul style="list-style-type: none"> • it is simple and easy to apply; • final stocks are evaluated at the latest values and are, therefore, closer to the economic reality
DISADVANTAGES	<ul style="list-style-type: none"> • the exits from stock are undervalued during the inflation period, witch lead to a minimization of costs and to the overvaluation of the final result; • opposite, the exits from stock are overvalued in a period of falling of the prices, so, the cost are delayed correlated with price variations;

Figure 3 Advantages and disadvantages of FIFO method

Sources: Iacob, Constanța, Ionescu, I., Avram, Marioara, 2012

In usage of FIFO method, the main disadvantage is that, during the inflation period, the gross profit and final entrance value of stock is higher. Taken into account the increase of the taxable base, that entity will pay to the state budget raised taxes, meaning tax on profit.

The method "*last in-first out*" (LIFO) enter's the alternative accounting treatment allowed [13] and assume the evaluation of goods out at the cost of production or acquisition of the last entry. The stocks out are considered as belonging to the last group entered in the warehouse and will be evaluated at its cost. Further, the outs of goods shall be considered as belonging to the previous group. By using this method it's reaced to an approximation of the costs to the latest operations to the results of the period. LIFO method generally requires complex calculations, and in practice there are various methods of applying the LIFO calculation formula. In some cases, LIFO's method formula can present serious problems in the application process, for example, when are new material products in order to replace other materials from the product, or when there are substantial liquidations of stocks as a result of the sale of a branch or subsidiary.

Due to the complexity LIFO method is not feasible, in general, to perform calculations within interim period during one year of financial reporting of the enterprise.

At international level, this method is used very often, because large entities although wish to obtain profit, have in mind the fact that, as higher is the profit, is higher the tax of profit increase. We believe that the LIFO method is a more realistic method, in case of measurements of flow of costs in the profit and loss account. Although it distorts the balance sheet because the remaining stocks are registered at a lower value, but conduct to a profit and loss account more correctly.

However, patrimonial economic units from our country have the opportunity to evaluate and registration in accounting, the goods such as stocks also to other prices, with the condition that in the periodic reports, they must be updated to actual costs. More specifically, these registration prices can be: default prices (standard) and billing prices.

International Accounting Standards IAS / IFRS do not allow the usage of LIFO method, for the determination of the cost of stocks

ADVANTAGES	<ul style="list-style-type: none"> • the exits from the stocks are evaluated at the most recent costs; • in times of inflation, the consumptions are overevaluated, compared to the FIFO method, which leads to an increase of the expenses and to a decrease of the results of the exercise, therefore, finally to a reduction of the tax on profit; • reverse phenomenon occurs in a period of falling of the prices
DISADVANTAGES	<ul style="list-style-type: none"> • costs are correlated with price variations, but the stock is underevaluated, in case of currency depreciation during the period of strong growth of the prices, entity, that can fix its sales prices, after full costs, is interested to follow that the sales prices to immediately follow its buying prices, so that the prices to generate a sufficient reserve to deal to purchases.

Figure 4 Advantages and disadvantages of LIFO method
Sources: Iacob, Constanța, Ionescu, I., Avram, Marioara, 2012

The LIFO method of stocks evaluation at the exit from the patrimony presents the following advantages and disadvantages according to the Figure 4 [13, 14, 15].

5. Conclusion

After analysis of the evaluation methods of stocks at the exit from patrimony, we found that the evaluation of stocks at the exit from patrimony is carried out using three methods, and each entity has the right to choose through which method can evaluate its stocks. The most common method is FIFO method, because economic agents prefer that profit to be very high.

Since 2015 it was passed to FIFO inventory evaluation method from CMP.

Regarding the application of the those three methods of evaluation of stocks at the exit from patrimony, in a case study conducted, using the same values, we have noticed that using different calculation methods also the values obtained will be different. In this case, the expense is different, influence primarily the profit.

Considering the advantages and disadvantages above mentioned, depending on the need of a firm, it can choose the appropriate method of evaluating the stocks at the exit from patrimony, according to the purpose pursued.

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