The Impact of Accounting Advances on the Valuation of Property and Liabilities of the Organization

A V Lapaeva¹, L E Tumali¹
¹Far Eastern State Transportation University, Russia

Abstract. The accounting statements of the organization made up in compliance with all the rules are perceived by interested users as a reliable information source especially if the auditor gave them a positive assessment implicitly. Only those who have a good understanding of the rules of Russian financial accounting know the intricacies of forming the organization’s statements that can distort the fair valuation of its property and liabilities.

Drawing up accounting records is one of such items of book records and tax accounting in the case of full or partial prepayment for products (services and work). Compliance with the accounting rules determines incomparability of payables in liabilities and receivables in the organization’s working capital due to the asymmetric inclusion of the sum of value added tax in these items of the balance sheet.

It is necessary to adjust the amount of receivables reflected in the balance sheet to understand the true value of the ratio of both debts, which determines the company’s paying capacity and the need for working capital, its financial stability and business activity.

1. Introduction
Assessment of the solvency and financial stability of the company, its financial obligations, receivables and payables, financial and business risks is carried out by third parties and financial managers, as a rule based on the information from the accounting (financial) statements (AFS). Professionals in the field of accounting and financial management, who know the official accounting rules and regulatory requirements for drawing up reports, are aware of certain situations when specifying business and financial transactions strictly according to legal standards one can get a paradoxical and distorted view of the AFS indicators valuation [1−4]. It can happen during accounting for advance payments. The estimated period of repayment of the company’s debts and the judgment about the turnover of outstanding liabilities of buyers and customers depends on how the value-added tax is taken into account in the case of an advance payment for goods and services. Without knowing the details of the agreements concluded between the parties, which provide for prepayment for products or services, a third-party user interested in the AFS may be misinformed regarding the actual amount of outstanding liabilities and the cost of working capital that the company actually has. If such a situation occurs, it is important for management personnel and AFS external users (potential investors, suppliers and contractors, policyholders and creditors) to know how to adjust the recorded values of receivables and payables in order to determine their reliable size and have a true idea of the company’s business activity.
2. The occurrence of a value assessment distortion of receivables when partial or full prepayment and VAT are indicated in the balance sheet

When the conditions of full or partial prepayment for products and services are included in a business agreement, current accounting rules [5, 6] require the counterparties to indicate the amount of this payment as receivables and payables. When transferring the amount of the advance, the amount of VAT in accounting may not be immediately shown as VAT on acquired values, because according to accounting rules the amount of recoverable taxes, which include the value-added tax (VAT), is not included in the value of the assets acquired by the organization on the terms of a preliminary payment.

The current accounting standards [7, 8] provide that if a company transfers payments (partial payments included) on account of the upcoming deliveries of goods (performance of work, rendering services and property rights transfer) they should be indicated in the balance sheet as receivables in the assessment, minus the amount of value added tax (VAT) which is deductible (accepted for deduction) in accordance with the tax legislation. A similar approach is used when indicating advances received from customers in accounts payable.

Accounting makes it possible to accept the “incoming” VAT on the amount of the advance for deduction in any reporting period at the discretion of the organization. At the same time, the Tax Code of the Russian Federation establishes requirements for organizations-sellers, namely upon receipt of payment (advance payment), to form tax arrears [9].

Eventually, the VAT charged on the amount of the advance is included in the balance sheet item, which is payables to the budget for taxes and fees [10].

At the same time, receivables indicated in the balance sheet as part of the property do not include the amount of VAT on the advance payments transferred by the suppliers.

As a result, the described approach to disclosing information about the status of the receivables concerning advances in the financial statements, leads to the incompatibility of its size with payables. AFS user is not able to compare them reliably, assessing the organization’s short-term solvency. It is difficult to understand the true size of obligations of counterparties who received an advance from it, and it is difficult to determine the type of financial stability [11]. The value assessment of the property, performed in full compliance with the regulatory requirements, turns out to be inaccurate and, therefore, efficiency indicators of working capital usage by business and company’s business activity calculated on its basis will not be true.

The need to adjust the amount of receivables to ensure the reliability of the management analysis results is obvious. It is required in the case of professional valuation of property, business and investment attractiveness of the company and in the case of usual reconciliation of obligations [12].

3. Adjustment of receivables in financial statements and changes in their estimated figures

3.1. The proposed method of adjustment of receivables

In order to form reliable information on the status of receivables, we consider it necessary and possible to adjust them by including the amount of VAT.

It should be noted that it is necessary to organize analytical accounting on sub-account 60 “Advances issued” in the context of value added tax in organizations that operate applying different VAT rates (20% and 10%), for the calculation accuracy of adjustment amounts [13].

We carried out research in a large organization of the gas distribution industry and tested proposals for adjusting the advances amounts in receivables. Table 1, given as an example, shows the results of the adjustment of receivables.
Table 1. Change in the receivables amount as a result of the adjustment.

| Indicator                          | Advances issued, excluding the amount of VAT, thousand roubles | Specific weight, % | Advances issued, adjusted for the amount of VAT, thousand roubles | Specific weight, % | Change in the amount, thousand roubles |
|------------------------------------|---------------------------------------------------------------|--------------------|---------------------------------------------------------------|--------------------|---------------------------------------|
| Long-term receivables              | 339                                                           | 0,003              | 339                                                           | 0,003              | 0                                     |
| Short-term receivables, incl. - buyers and customers | 11 174 880                                                   | 99,997             | 11 704 823                                                   | 99,997             | 529 943                               |
| - advances issued                  | 3 521 485                                                     | 31,513             | 3 521 485                                                     | 30,086             | 0                                     |
| - other debtors                    | 2 944 127                                                     | 26,346             | 3 474 070                                                     | 29,681             | 529 943                               |
| Total accounts receivable          | 11 175 219                                                    | 100                | 11 705 162                                                    | 100                | 529 943                               |

The results of the adjustment lead to the conclusion that changes in the amount and structure of the receivables are noticeable. The total amount of the receivables increased by about 5%, which is significant from the point of view of the rules for the formation of the AFS indicators [14].

3.2. Change in key financial ratios of solvency and business activity after the adjustment of receivables

After the VAT amount was added to the amount of issued advances the total amount of receivables increased, that also changed the ratio of receivables and payables indicating paying capacity and their turnover periods, characterizing the efficiency.

Table 2. Comparison of changes in debt ratio.

| №     | Indicator                                      | On 31.12.201 | On 31.12.2016 | Change |
|-------|-----------------------------------------------|-------------|--------------|--------|
| 1     | Ratio of receivables and payables before the adjustment | 0,763       | 1,246        | 1,494  | 0,732  |
| 2     | Ratio of receivables and payables after the adjustment | 0,776       | 1,234        | 1,513  | 0,737  |

The impact of the adjustment on the balance sheet is even more noticeable when comparing the turnover periods of receivables calculated before and after the adjustment.
Table 3. Comparison of the turnover periods of receivables before and after adjusting the advances issued for the VAT amount.

| №   | Indicators                                                                 | On 31.12.2015 | On 31.12.2016 | On 31.12.2017 | Change 2017-2015 |
|-----|-----------------------------------------------------------------------------|---------------|---------------|---------------|------------------|
| 1   | Turnover period of receivables before adjusting the advances issued for the amount of VAT | 92,028        | 96,091        | 90,107        | -1,921           |
| 2   | Turnover period of receivables                                             | 96,087        | 100,329       | 94,081        | -2,006           |

It is obvious that the turnover period increased every year by approximately the same value of 4 days over the course of all three years. If we evaluate its absolute changes over the three years from December 31, 2015 to December 31, 2017 in the two variants of the receivables amount, we should note the almost unchanged value of the dynamics indicator.

Thus, the proposed option of adjusting receivables causes an increase in their turnover period, a change in their relation to payables, and, therefore, changes the AFS user’s perception of a number of financial criteria.

4. References

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