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ACCOUNTING JUDGMENTS AND RULES ON THE OUTCOME OF THE AUDITED ENTITY'S ACTIVITY DEPENDING ON THE INCORPORATED/ UNINCORPORATED EXPENSES IN THE COST OF PRODUCTS

Assoc. prof. Camelia Cătălina MIHALCIUC[1]*, Economist Aurelian BACINSCHI[2]
[1] Universitatea Ştefan cel Mare Suceava, e-mail: cameliam@seap.usv.ro
[2] Camera de Conturi Suceava, e-mail: aurelian.bacinschi@yahoo.com

Abstract
In the Romanian accounting system, the costs incurred for obtaining the products (assimilated here: semi-finished products, finished products, residual products, agricultural products, products in progress) are compensated by registering of certain incomes when they are handed over to the warehouse, and then adjusted registering price differences at the end of the month. Due to this fact and to the more complex function of the account 711 - "Revenues related to product inventory costs", the auditing of finished product accounts, of price differences in finished products accounts and of related revenues (acc. 711), usually present a high degree of risk. Also, the specificity of these accounts requires a good knowledge of the system used to calculate production costs, respectively of correctly identifying the categories of expenses which will be included/not included into the cost of the products. Thus, in the present study, the main objective aims to establish certain working hypotheses, which identify situations related to the inclusion/non-inclusion of the certain expenses in the cost of the products, that will influence the result of the activity (taking into account the present laws) and based on the stated hypotheses to draw the related rules.

Key words: *included expenses, non-included expenses, additional expenses, cost of products inventories*

JEL Classification: M410 Accounting, M420 Auditing

* *Camelia Cătălina MIHALCIUC, e-mail:* *cameliam@seap.usv.ro*

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I. Introduction

Most often, the post calculation (determining the actual cost of production) starts from the total expenses registered in the financial accounting (class 6), from which the non-incorporable expenses are eliminated and the additional expenses are added.

Because the value of the finished products is determined by the summarization of the balances of the accounts 345 – *Finished products* and 348 – *Price differences related to finished products* resulting a value at the actual cost, and the account 331 – *Products in progress* is also registered at the actual cost, it results that for the auditor is it is very important to investigate how to determine the actual cost within each audited company. For this reason, it is also justified to classify expenditures in terms of incorporation / non-incorporation in the cost of products, with production costs comprising only those costs that are related to the activity carried out to obtain production over a certain period of time being admitted as such, by the legislation in force.

II. Aspects related to the categories of expenses that may be included in the cost of production

OMFP 1802/2014 stipulates the categories of expenses that should not be included in the cost of inventories, but will be recognized as expenses in the period in which they occurred. It is thus shown that material losses, labor costs or other costs of production over the normal values, including losses due to waste, are not included in the cost of inventories. Starting from these provisions, it is noticed the importance of accurately identifying the nature of the loss, because depending on this, there will be different influences on the cost of the products, the regular losses affecting the cost of the stocks, the abnormal ones being only expenses of the period, and the expenses capitalized by selling or internal use, are as well as affecting the cost of the products inventory.

Also, storage costs, unless these costs are necessary in the production process before the start of a new manufacturing stage (storage costs necessary to bring the inventory into the place and the state they are in), are not part of the cost of production. Other expenses that cannot be included in the cost are general administrative overheads that do not participate in bringing the inventory to the final form and place, as well as fixed unallocated overheads, which is registered as an expense in the period in which it occurred.

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From these aspects, a particularly sensitive issue is the ratio between the expenses recorded in the financial accounting by their economic nature and the costs incorporated in the cost of production, which is subject to management accounting, on the basis of which, the expenses being delimited in three categories:

1. *a. Expenses incorporable in production costs (calculated expenses),* which comprise costs dependent on the cost of production, consisting of operating expenses, recorded as such in financial accounting by their economic nature

For the purpose of calculating production costs, expenses recorded in financial accounting by their nature, may be grouped into the management accounting according to the destination criterion in direct production costs, indirect production costs, selling expenses, general administration expenses.

The incorporable expenses from financial accounting are taken into consideration by the management accounting entirely, by including them into production costs, thus forming the section costs, but it does not allow for the normal operating conditions to be emphasized, or it does not always reveal the performance or shortcomings in the activity. So, we can speak of another category, namely those expenses partially included in costs, which are considered in management accounting at a value different from the one recorded in the financial accounting, depending on the degree of fulfillment of certain reference parameters. We can say that it is attempted to replace the expenses calculated according to the fiscal requirements with the ones that correspond to the economic criteria and which correctly reflect the reality, as for example the case of indirect costs that are partly included in the cost of production (equipment depreciation expenses), included in cost based on the number of hours worked. As a result, the cost does not necessarily include all the expenses recorded in the financial accounting according to fiscal criteria, but according to the hours worked by the machine.

2. *b. Expenses non-incorporable into costs,* those recorded in financial accounting by their economic nature but not includable in production costs because they do not condition the realization of products, works or services.

Expenses from financial accounting which are not part of the cost of production are those not directly related to the company's operations (fines, discounts, penalties, other financial expenses, excluding interest on loans for long-term manufacturing facilities, which may be allocated to the production costs of the products concerned); are not a result of current activity (expenses incurred as a result of unfortunate events recorded as other operating expenses); they do not have the characteristics of regular expenses (profit tax

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expense), or the expenses provided in OMFP 1802/2014, presented at the beginning of point 1 of this study.

c. Additional expenses (supplementary), being those costs that are not subject to financial accounting, in order not to affect the corporate tax, but are considered elements of cost in the management accounting.

These types of expenses may include: the remuneration of the individual entrepreneur (the amount paid to the person benefiting from a share of profit and not a salary, which is an expense and therefore an element of the cost); the remuneration of own capital, which must be taken into account in the calculation of the costs, regardless of its nature: owned or borrowed; product research expenditure (ex. developing a proprietary product within a 4-year period; the research expenses were made during the design phase of the product and they were recorded directly in the expense accounts without capitalizing, until the moment of production start, they were non-incorporable costs, during the life of the product these costs were not recorded in the financial accounting, they are included in the cost of the product as additional expenses).

Taking into account all these aspects, it can be seen that, in order to determine the full commercial cost, on the one hand it is based on the expenses recorded in the financial accounting, and on the other hand, corrections have to be made regarding the elimination of the non-includable expenses; the incorporation of certain expenses to a value other than that recorded in financial accounting or management accounts.

III. Statements and rules starting from the inclusion/non-inclusion of expenses into the cost of products

Hypothesis 1: the company carries out activity, registers finished products but does not sell during the month, only expenditures that can be incorporated into the cost of the products according to the law are made;

Rule 1: If the expenses incurred during a period are entirely inccludable in the cost of the products and during that period the company sells nothing, the result of its activity is equal to 0 (the revenues being equal to the expenses).

Hypothesis 2: the company carries out activity, registers finished products but does not sell*; during the month legally includable expenses are made, but also non-includable expenses reprezented by interest of a few lei;*

Rule 2: If, in the course of a period part of the expenses are non-includable, and during that period the company sells nothing, the result of the activity will be a loss equal to the amount of non-includable expenses.

Thus, if it is used correctly, the account 711 - "Revenues related to product inventory costs", cannot generate profit, through the way the values of the registrations in which it is used are determined. It is only a revenue account that is designed to compensate the actual cost of production.

Based on this reasoning, we can also formulate the following rules:

Rule 3: If, during a period, only incorporable expenses are incurred and during that time the company sells finished products at a price higher than the actual cost of production, the result of the activity will be a profit of a size equal to the difference between the sales revenue and the actual cost of the products sold.

Rule 4: If, during a period, both includable and non-includable expenses are recorded, and during that time the company sells finished products at a higher price than the actual production cost (no other revenues are recorded), the result of the activity can be determined based on the following relationship:

Result = (Sales revenues) – (Cost of sold products) – (Non-includable expenses)

Hypothesis 3: A company produces long-cycle manufacturing goods; a single unit is being launched and the second one will be launched in the fourth month; suppose it is the first month of activity and the product will be completed within 2.5 months (the finished product will be received in the 3rd month); only includable expenses are recorded; until the sale (during the 3rd month), no income from other activities are recorded;

Rule 5: Current credit amounts of account 711 related to the reception of finished products during the period (at standard cost)

(+/-) Current amounts of account 711 related to the price differences of the received finished products

(+) Current credit amounts of account 711 related to the production in progress at the end of the period

<u>(-) Value of the production in progress at the end of the previous period</u>

= Totalul includable expenses registered during the audited period

If the total incorporable expenditure over a specified period, based on the balance of accounts, is less than the total value of records 345 = 711, 348 = 711 and 331 = 711 minus the value of the production in progress at the end of the previous period, then the company has artificially increased the result through these operations. If the total includable expenses are lower, then the company has artificially diminished its result during that period. Suggestively this comparative calculation can be highlighted in Figure no. 1:

Figure no. 1. - Comparable elements with influence on the result

TOTAL INCLUDABLE EXPENSES DURING A PERIOD	> <	Current amounts of account 711 related to the reception of finished products + Current amounts of account 711 related to the the price differences of the received finished products + Current amounts of account 711 related to the production in progress - Final balance of account 711 at the end of the previous period

Source: Personal elaboration

The calculation of the "K" coefficient for removing the cost differences of the products sold: K = (Initial balance of acc. 348 + its current amounts for received finished products) / (Initial balance of acc. 345 + its cumulated amounts of received finished products since the beginning of the year).

Rule 6: In the case of a company which uses the formula for calculating the difference in cost for sold finished products "K" as a formula that takes into account the final balances of accounts from the previous month and the amounts of the current month, at each end of the month the following correlation should be valid: (Final balance of 345) x (K for the respective month) = Final balance of 348

IV. Conclusions

Starting from all these hypotheses and rules presented in the study, we can see the importance of knowing the system of calculating production costs, by correctly identifying the categories of expenses that are to be incorporated/not incorporated into the cost of the products that will subsequently affect the result of the activity.

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