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Analysis of Financial Accounting Information Relevance in the Banks

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Abstract: *Specific to banking companies is the way of developing the business activity while maintaining confidence in the monetary system, and deepening relationships with the banking supervisory authority and other state authorities. Given the need for savings with the intermediation of investment into monetary instruments, a considerable interest arises for the operation of banks. We consider mainly solvency, liquidity and the degree of relative risk for various activities they perform. In this context, presenting analyzes of financial statements reflecting aspects such as the management and control of liquidity, significant risks, is essential for both customers and for bank supervisors.*
Keywords: *a monetary system, a financial position, quantifiable risks, an individual performance, a contingencies and commitments*

Introduction

Users of financial statements of a bank need relevant, reliable and comparable information to help assess the bank's financial position and performance, information that is useful for making economic decisions. Also, there is a lot of other information to help them understand the special characteristics of a bank's operations. In practice, even if a bank is supervised by regulatory authorities and by independent auditors, information about their financial position is not always publicly available. Therefore, information presented in the financial statements of a bank must be sufficiently complete to meet the needs of users, in the limit of what can reasonably be called leadership.

The main recipients of a bank's financial statements are interested in the liquidity and solvency and risks of its assets and liabilities recognized in the balance sheet or balance sheet items. Liquidity refers to the availability of sufficient funds to meet withdrawals of deposits and other financial commitments when they fall due, and solvency concerns the extent to which assets exceed liabilities and the capital adequacy of banks.

1. Financial Statements and Relevant Information

The main risks faced by a bank that users want to quantify them are related to liquidity, exchange rate variations, changes in interest rates, changes in market prices and non-compliance by the partners. These risks may be reflected in financial statements, but users will get a better understanding of them only to the extent that management has in addition and description of administration and control of risks associated with bank operations.

In terms of accounting policies, banks use different methods for recognition and valuation of their financial statements, a standard for their harmonization is not yet implemented. Because users can assess the relevance of the information disclosed in financial statements is required accounting policies used by the bank on the following aspects:
- how to recognize the main types of income;
- how to assess investment securities and marketable securities;
- transactions recognized in the balance sheet commitments reflected elsewhere;
- present and potential losses from loans and advances;
- effects production costs cover significant risks.

The bank profit and loss must cover income and expenditure by nature and present value of the main types of income and expenses, as follows:
- interest income and similar income;
- interest expense and similar charges;
- dividend income;
- income from fees and commissions;
- fees and commissions;
- net gains on trading securities;
- net investment securities gains;
- net gains from foreign currency transactions;
- other operating income;
- losses on loans and advances;
- general administrative expenses;
- other operating expenses.

The major categories of revenues generated from operations of a bank are of interest, service charges, commissions and income from transactions, each of which must be shown separately, so that users can assess the performance of banks.

The main types of costs arising from operations of a bank include interest, fees, losses on loans and advances, expenses reduce the carrying amount of investments and general administrative expenses. Each type of expense should be presented separately so that users can assess the performance of banks.

Income and expense items should not be offset except for those related to hedging transactions, since this compensation prevents users to evaluate the performance of individual activities of a bank and you get return on various asset classes. Ultimately, the net gains or losses are reported in operations with trading securities, transfers of investment securities and foreign currency transactions.

Interest income and interest expense should be presented separately for a better understanding of the structure of net interest and the reasons which determine amendment. Since net interest depends on the interest rates and the amounts raised and borrowed, is the submission of details of average interest rates, average assets and interest bearing interest-bearing liabilities for the period analyzed.

Within the balance sheet, assets and liabilities are grouped according to their nature and listed in an order that reflects their relative liquidity. These relate mainly to:
- a cash and balances with central bank;
- securities and other securities may be presented for re-evaluation at central bank;
- securities and other securities held for trading;
- placement to other banks and loans and advances to other banks;
- other money market placements;
- loans and advances to customers;
- investment securities;
- other bank deposits;
- other money market deposits;
- an amount owed to other depositors;
- a certificate of deposit;
- promissory notes and other liabilities certified documents;
- other borrowed funds.

2. **Classification of Bank Assets**

In most cases, classification of assets and liabilities of a bank is in their nature, then the approximate order of their liquidity and ultimately the extent of their maturities. Usually, items short and long term are not presented separately because most assets and liabilities of banks can be realized or settled in the near future. In the balance sheet, the amounts recorded in accounts with banks and financial customers are reflected separately from those of other depositors because it is essential to highlight the bank's relations with other banks and money market and bank dependence that is subject to them. So distinct are the central bank balances, investments in other banks, other money market placements, and deposits from other banks, other money market deposits and other deposits received.

In practice, the value of any asset or liability presented in the balance sheet should not be compensated by deduction other asset or liability, unless the compensation is the prospect of realization or settlement of assets and liabilities.

Quotas and commitments contained in the passive should be grouped as follows:
- where nature and amount of credit irrevocable commitments;
- direct credit substitutes;
- guarantees to customers (performance, to participate in tenders, letters of credit);
- revocable and irrevocable documentary credits;
- foreign exchange operations related to interest rate and exchange;
- other given commitments.

There are cases of transactions that do not entail immediate registration of assets or liabilities on the balance sheet, but give rise to contingencies and commitments. Of these, off-balance sheet items is a very important part of bank activity, with major implications on the overall risk they are exposed. For this reason, as users of financial statements to be informed of the contingencies and irrevocable commitments of a bank, because the effects they have on bank liquidity and solvency and the inherent possibility of occurrence of potential losses. Users must have also information on the nature and amount of off-balance sheet transactions conducted by a bank.

Provide an analysis of assets and liabilities broken down by final maturity is essential to establish correlations between the maturities and interest rates on bank assets and liabilities. This analysis is fundamental for both bank management and their customers, because in practice it is almost impossible to achieve a position of perfect correlation, banking were often uncertain maturities. However, maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing a bank's liquidity and its exposure to changing interest rates and exchange rates. To provide relevant information as possible about the liquidity forecast, the bank should have at least an analysis of assets and liabilities broken down into relevant maturity period.

Various maturity periods of active and passive applied varies from one bank to another and are more or less appropriate certain assets and liabilities because they are frequently combined. For example, loans and advances shall be grouped into two categories: under a year and a year and where repayment is spread over a longer period, each installment is allocated to the period of the contract was agreed or expected to be paid or collected.

It is essential that the maturity periods adopted by a bank be the same both for assets and liabilities. This clarifies the extent to which the maturities of assets and liabilities are related and whether the bank depends on other sources of liquidity.

Because certain assets of a bank do not have a contractual maturity, may be taken their maturity, regarded as the date at which those assets are expected to be made.

In cases where a bank's liquidity is assessed on the outstanding groups take into account first the availability of the market money or, in case of emergency, from the central bank. For proper understanding of the maturity groups, it is useful to present information on the likelihood of repayment period until maturity, so the effective periods and how to manage and control risks and exposure to risk associated with different profiles on the maturity and interest rate.

Some of the most complex and difficult aspects to be quantified are the significant assets concentrates, liabilities and off balance sheet items, the rationale behind quantifying the level of risk that is subject to bank. Such information must be presented by geographic areas, groups of customers or sectors or according to other risk concentrations. Geographical areas may include countries, groups of countries or regions within a country, presenting customers may reflect sectors such as governments, public authorities, commercial enterprises and other enterprises.

Information on significant net foreign currency positions provide useful clues about the risk of losses arising from changes in exchange rates.

In terms of losses on loans and advances, you must submit the following information:
- the accounting policy for the recognition of the costs and passing on losses of the loans and non recuperated advances;
- details of movements a provision for losses on loans and advances during the period;
- an aggregate amount of provisions for losses on loans and advances at the balance sheet date;
- a total amount included in the balance sheet for loans and advances that stopped calculating and recording interest on the method used for determining the carrying amount of such loans and advances.

All amounts, provided as reserves for losses on loans and advances, in addition to specifically identified losses or potential losses to be identified from experience in portfolio loans and advances, shall be accounted for as appropriations of retained earnings because any amount credited due to the reduction of such amounts increase the retained earnings and not included in determining net profit or net loss for the reporting period.

It is inevitable that in the ordinary course of business banks to record losses on loans, advances or other credit facilities that are partially or fully recovered. The losses value, specifically identified, is recognized as an expense and deducted from the carrying amount of the corresponding category of loans and advances as a provision for losses on loans and advances. The potential losses value, that can not be specifically identified, may be recognized as an expense and deducted from the total book value of loans and advances, and provision for losses on loans and advances. Evaluation of these losses depends on management judgment and it is essential that they be applied consistently from period to period.

Market conditions or legislation may require or allow a bank to make reserves for losses on loans and advances over the losses identified specific losses which experience indicates as being present in the portfolio of loans and advances. All the reserves are appropriations of retained earnings and are not counted as expenses in determining net profit or net loss for the period. Similarly, any amounts recognized as reserves such reductions lead to increased retained earnings and not included in determining net profit or net loss for the period.

Users of financial statements of a bank must know the impact of losses on loans and advances have had on the financial position and results of the bank because they can better assess the effectiveness of the bank have used the resources. Therefore, a bank should present total provision for losses on loans and advances at the balance sheet and movements in provision during the period. Evolution provision, including values that were passed earlier losses and were recovered during the period must be presented separately.

Total loans and advances on which interest is not calculated and the method for determining the carrying amount of these loans and advances should be detailed and specified that recognizes interest income on such loans and advances and the impact that the non-calculating the interest has on the profit and loss.

If loans and advances are stranded, they have written off, less provision constituted for this purpose. In other cases they can be written off earlier, for example, when the debtor has not paid interest and repaid the outstanding capital during a given period. Because when irrecoverable loans and advances are written off differs, the gross loans and advances and provisions established for these products may vary considerably in similar circumstances, it is essential for the provisions.

Provisions, and any reserve for general banking risks, should be presented separately as appropriations of retained earnings. Any changes resulting from such reduction leads to increase reserves and retained earnings should not be included in determining net profit or net loss for the period. The main motivation for this operation resulting from the need to avoid an excessive size of assets and liabilities, failure costs incurred and bank reserves and likely to distort net income and equity.

Profit and loss account can not provide relevant and reliable information on the performance of a bank if net profit or net loss for the period includes the effects of established reserves for general banking risks or additional contingencies, or credits resulting from reversal of such reserves. Similarly, the balance can not provide relevant and reliable information on the financial position of a bank if it includes overstated liabilities, understated assets or undisclosed expenses incurred and provisions.

Conclusions

Today, according to their object of activity, banks frequently conduct a management activity or one of an investment consultant which involves holding or placing of assets on behalf of individuals, trust funds, pension plans and other institutions. Since in this case, the bank acts only as an administrator, those assets do not belong to the bank and therefore should not be included in the balance. However, if the bank is significantly involved in assets management activities, financial statements should disclose that fact, through explanatory notes, thoroughly presenting the liabilities that could arise if the bank fails to follow its administrative responsibilities.

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