

EARNINGS AND FAIR VALUE ACCOUNTING

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Abstract

Fair value measurements are on the Romanian Commercial Bank earnings at June 30, 2019. We focus on the relationship between fair value measurements and predictability as a measure of earnings quality. The data collected are from the Romanian Commercial Bank annual reports at June 30, 2019. The persistence, predictability, accruals quality, earnings smoothing and value relevance are the most important measures of earnings quality. Earnings quality and the quality of accounting information are in direct relation. The usefulness of fair value information is explored directly by inspecting its predictive power with respect to future cash flows and future earnings.

Keywords: *earnings quality, earnings predictability, commercial bank, fair value accounting, financial statements, historical cost.*

1. Introduction

Johnson et al.¹ stated in 1995 that financial failure was not reported and thus was ignored on the condition that these securities were still being held, yet according to Johnson profits could be reported for securities rising values. Then, the controversial use of FVM, he establishes a direct connection between Enron's collapse, the GFC, and improper FVM practices. Secondly, the current pricing strategy for audit as an industry response to the abuse of external audit arrangements. Based on the comprehensive literature review, Johnson arrives at two earlier main findings. For this reason, FVA in the early 1990s was put forward as a remedy, so that losses as well as profits could be accounted for in a timely and honest way.

There was no noticeable change in these requirements when they began in 1993 until after the GFC in 2008-2009. Other fair value standards, also comprising mixed forms of measurement, soon followed FAS 115, for example FAS 123: Accounting for Stock-Based Compensation (FASB, 1993), and FAS 133: Accounting for Derivative Instruments and Hedging Activities (FASB, 1998). The standards represented efforts to prepare fair values through the profit statement in specific scenarios. In 1998, IAS 39 was established by the IASB. At that time, IASB standards were referred to as International Accounting Standards (IAS). Subsequently, FAS 115 was equivalent to IAS 39: Financial Instruments: Recognition and Measurement, (IAS Plus 2019). In fact, IAS 39 and FAS 115 were similar in adopting a mixed approach (both fair value and historical cost models).

Heaton et al.² established in 2010 that regulators noted the rise of financial instruments and wanted a

method with which to measure those financial assets that were being rapidly traded fairly. Then we noted the FAS 115: Accounting for Certain Investments in Debt and Equity Securities (FASB, 1993).

Schultz and Hollister remarked in 2003 that following pressure by conservative banks, the standard only needed some investments, in other words, those proposed to be sold in the short-term and those prepared using fair value through the profit statement.

Chen, Lo, Tsang & Zhang, in 2013, established that earnings quality is used as an indicator of dividends, as these dividends are important things that are taken into account when making investment decisions.

Sodan said in 2015 that the fair value approach is also one of the approaches that was born to cover the shortcomings of applying the historical cost approach. This approach shows users of financial statements the right information to make the right decisions, because that information becomes more relevant when we apply fair value.

1.1. Earnings and fair value

After Sodan (2015), his concept of valuation was adopted, as he mentioned that exposure to fair value accounting is measured using global or net income approaches. In other words, changes in fair values are reported as gains and losses on net or other global income.

Thus, we deduced that the effect of gains (losses) on fair value through other comprehensive income and net income on predictability as a measure of the quality of gains. Muller, Riedl & Sellhorn, in 2008, analysed the historical cost principle, which led them to look for a new accounting alternative to keep up with the economic conditions characterized by Asian Economic and Financial Review, 2020, 10 (12): 1466-1479 1468,

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¹ Johnson, E. N., Walker, K. B., & Westergaard, E. (1995). Supplier concentration and pricing of audit services in New Zealand. *Auditing*, 14(2), 74.

² Heaton, J. C., Lucas, D., & McDonald, R. L. (2010). Is mark-to-market accounting destabilizing? Analysis and implications for policy. *Journal of Monetary Economics*, 57(1), 64-75. <https://doi.org/10.1016/j.jmoneco.2009.11.005>.

which cause strong fluctuations, changes in purchasing power, create instability and lead to inflation or depression. It is undeniable that the concept of fair value has projected traditional accounting theory to new horizons and brought a comprehensive innovation in the structure of financial statements and their implications. This has been an effect of the evolution of accounting theory in recent years, which have matured and been implemented in international fair value accounting standards and was introduced at the beginning of the third millennium, in 2001 (Sodan, 2015). When a company uses the fair value method, it generates higher income due to the difference between the fair value and the carrying amount, which is recognized as part of the gain and loss on the application of fair value. Thus, using the cost model, the value of net income or loss is distorted only by depreciation expenses (Wahyuni, Soepriyanto, Avianti and Naulibasa, 2019).

2. The fair value of financial assets and liabilities at Romanian Commercial Bank

Romanian Commercial Bank was established in 1990, when it took over the commercial operations of the National Bank of Romania.

Fair value is the price that would have been collected for the sale of an asset or paid for the transfer of a debt in a regulated transaction between market participants at the valuation date. The fair value is best highlighted by a price dictated by the market, if it exists. The value adjustments due to changes in credit risk is included in the fair value of derivatives and is intangible both on December 31, 2018 and on December 31, 2019.

Level 1 in the fair value hierarchy

The fair value of financial instruments allocated on level 1 of the fair value hierarchy is determined on the basis of the prices quoted on the active markets related to identical financial assets and liabilities. In particular, the measured fair value can be classified as entry level 1 if the transactions take place with a high frequency, volume and consistency of pricing continuously. This will be used as a fair value and in this case no valuation model is needed.

These include derivative financial instruments traded on the stock exchange (futures contracts,

options), shares, government securities, as well as other bonds and funds, which are traded on highly liquid and active markets.

Level 2 in the fair value hierarchy

If a market quotation is used for valuation, but due to limited liquidity, the market does not qualify as active (information derived from available market liquidity indicators), the instrument is classified as level 2. If there are no market prices available, fair value is measured using valuation models based on observable market data. If all input data significant in the valuation model are observable, the instrument is classified as level 2 in the fair value hierarchy. For valuations for level 2, yield curves, credit margins and implicit volatilities are usually used as market parameters.

Level 2 includes financial instruments on the OTC market, less liquid shares, bonds and funds, as well as own issues. If the "spread" is not observable, it must be tested if the unobservable input parameter is significant. An unobservable input parameter for securities with theoretical prices is considered significant if the effect of unobservable inflows on the fair value of that guarantee is greater than 2%.

Level 3 in the fair value hierarchy

In some cases, fair value cannot be determined either on the basis of quoted market prices with sufficient frequency or on the basis of valuation models that take into account only observable market data. In these cases the individual evaluation parameters, unobservable on the market, are estimated based on reasonable assumptions. If significant strength data are not observable or the price quotation used is not frequently updated, the instrument is ranked level 3 in the fair value hierarchy. For level 3, the assessments take into account, in addition to observable parameters, credit margins derived from internal historical estimates for the probability of default (PD) and loss in case of default (LGD) which are used as unobservable parameters.

Financial instruments measured at amortized cost in the statement of financial position whose fair value is presented in the following notes.

The following table shows the fair value and the fair value hierarchy for financial assets whose fair value is presented in the notes to the financial statements at June 30th, 2019:

Figure 1. Statement of financial position



STATEMENT OF FINANCIAL POSITION

Consolidated and Separate

As at 30 June 2019

Statement of financial position

in RON thousands	Notes	Group		Bank	
		30.06.2019	31.12.2018	30.06.2019	31.12.2018
Assets					
Cash and cash balances	3	10,346,352	11,123,191	10,179,024	10,862,852
Financial assets held for trading		160,703	213,965	161,298	214,092
Derivatives		59,543	31,062	60,138	31,189
Other financial assets held for trading		101,160	182,903	101,160	182,903
<i>thereof pledged as collateral</i>		4,181	-	4,181	-
Non-trading financial assets at fair value through profit or loss		37,263	39,395	37,030	39,152
Equity instruments		33,048	33,475	32,815	33,232
Loans and advances to customers		4,215	5,920	4,215	5,920
Financial assets at fair value through other comprehensive income	4	5,458,119	5,222,081	5,412,021	5,187,019
Equity investments		54,178	40,721	54,178	40,721
Debt securities		5,403,941	5,181,360	5,357,843	5,146,298
<i>thereof pledged as collateral</i>		25,399	-	25,399	41,748
Financial assets at amortised cost	5	51,798,643	50,843,219	49,738,874	48,732,568
<i>thereof pledged as collateral</i>		806,426	690,952	2,097,320	1,693,280
Debt securities		15,299,100	15,879,108	14,066,921	14,297,905
Loans and advances to banks		269,108	123,840	280,364	388,848
Loans and advances to customers		36,230,435	34,840,271	35,391,590	34,045,815
Finance lease receivables		1,062,774	990,868	3,241	-
Property and equipment		1,077,677	1,169,260	974,754	760,646
Investment property		147,977	162,806	147,977	162,806
Intangible assets		345,856	361,898	339,630	354,020
Investments in joint ventures and associates		23,388	20,027	17,035	7,509
Current tax assets		200,258	181,800	197,295	178,822
Deferred tax assets		173,874	202,165	164,713	197,061
Assets held for sale		548,626	161,114	106,337	117,699
Trade and other receivables		490,654	563,014	480,201	543,179
Investments in subsidiaries		-	-	403,152	403,152
Other assets		346,768	275,502	185,649	148,677
Total assets		72,218,932	71,530,305	68,548,231	67,909,254

in RON thousands	Group		Bank	
	30.06.2019	31.12.2018	30.06.2019	31.12.2018
Liabilities and Equity				
Financial liabilities held for trading	83,128	32,988	83,128	32,988
Derivatives	83,128	32,988	83,128	32,988
Financial liabilities measured at amortised cost	61,890,320	61,618,808	58,881,083	58,326,984
Deposits from banks	6	5,294,492	4,562,358	4,791,204
Deposits from customers	7	55,427,344	53,150,871	52,593,690
Debt securities in issue	8	269,613	269,613	349,153
Other financial liabilities		898,871	898,241	592,937
Finance lease liabilities		249,912	245,567	-
Provisions	9	1,753,037	1,400,326	1,120,255
Current tax liabilities		4,051	-	97,110
Deferred tax liabilities		6,791	-	-
Liabilities associated with assets held for sale		35,499	-	15,438
Other liabilities		319,411	248,902	193,842
Total equity	7,876,783	8,366,714	7,689,225	8,138,075
Share capital	2,952,565	2,952,565	2,952,565	2,952,565
Retained earnings	3,255,783	3,766,482	3,051,869	3,525,615
Other reserves	1,668,435	1,647,667	1,684,791	1,659,895
attributable to non-controlling interest	52	46	-	-
attributable to owners of the parent	7,876,731	8,366,668	-	-
Total liabilities and equity	72,218,932	71,530,305	68,548,231	67,909,254

Source: https://cdn0.erstegroup.com/content/dam/ro/bcr/www_bcr_ro/EN/Investors/Financial-reports/2019/Financial_statements_June_30th_2019.pdf.

Figure 2. Statement of financial position (continued)

The fair values of loans and advances granted to customers and credit institutions have been calculated by discounting future cash flows taking into account the effect of interest and credit margin. The impact of the interest rate is based on movements in market interest rates, while credit margins are determined by the

probability of default (PD) used for the internal risk calculation. For the calculation of fair value, loans and advances were grouped into homogeneous portfolios, based on rating methods, rating class, maturity and client's country of residence.

The fair value of amortized cost financial assets is either taken directly from the market or determined by directly observable input parameters (i.e. yield curves).

The fair value of the securities issued and of the financial debts valued at amortized cost, is based on prices quoted in the active market of some similar tools. If these are not available and other observable input

parameters are used (e.g. quoted prices in inactive markets) the classification will be Level 2.

The fair value of deposits and other financial liabilities measured at amortized cost is estimated taking into account the market interest rate and credit margins; they qualify on Level 3.

20.2. Financial instruments measured at fair value in the statement of financial position

Group									
in RON thousands	Quoted market prices in active markets Level 1		Marked to model based on observable market data Level 2		Marked to model based on non-observable inputs Level 3		Total		
	30.06.2019	31.12.2018	30.06.2019	31.12.2018	30.06.2019	31.12.2018	30.06.2019	31.12.2018	
Assets									
Financial assets - held for trading	101,160	178,095	57,355	33,738	2,188	2,132	160,703	213,965	
Derivatives	-	-	57,355	28,930	2,188	2,132	59,543	31,062	
Other financial assets held for trading	101,160	178,095	-	4,808	-	-	101,160	182,903	
Non-trading financial assets at fair value through profit or loss									
Equity instruments	-	2,400	2,548	-	34,715	36,995	37,263	39,395	
Loans and advances	-	-	-	-	4,215	5,920	4,215	5,920	
Financial assets at fair value through other comprehensive income	5,350,969	5,031,042	45,627	144,301	61,523	46,738	5,458,119	5,222,081	
Equity instruments	-	-	-	-	54,178	40,721	54,178	40,721	
Debt securities	5,350,969	5,031,042	45,627	144,301	7,345	6,017	5,403,941	5,181,360	
Total assets	5,452,129	5,211,537	105,530	178,039	98,426	85,865	5,656,089	5,475,441	
Liabilities									
Financial liabilities - held for trading	-	-	83,128	32,988	-	-	83,128	32,988	
Derivatives	-	-	83,128	32,988	-	-	83,128	32,988	
Total liabilities	-	-	83,128	32,988	-	-	83,128	32,988	
Bank									
in RON thousands	Quoted market prices in active markets Level 1		Marked to model based on observable market data Level 2		Marked to model based on non-observable inputs Level 3		Total		
	30.06.2019	31.12.2018	30.06.2019	31.12.2018	30.06.2019	31.12.2018	30.06.2019	31.12.2018	
Assets									
Financial assets - held for trading	101,160	178,095	57,950	33,864	2,188	2,133	161,298	214,092	
Derivatives	-	-	57,950	29,056	2,188	2,133	60,138	31,189	
Other financial assets held for trading	101,160	178,095	-	4,808	-	-	101,160	182,903	
Non-trading financial assets at fair value through profit or loss									
Equity instruments	-	2,400	2,549	-	34,481	36,752	37,030	39,152	
Loans and advances	-	-	-	-	4,215	5,920	4,215	5,920	
Financial assets at fair value through other comprehensive income	5,350,969	5,031,042	-	109,239	61,052	46,738	5,412,021	5,187,019	
Equity instruments	-	-	-	-	54,178	40,721	54,178	40,721	
Debt securities	5,350,969	5,031,042	-	109,239	6,874	6,017	5,357,843	5,146,298	
Total assets	5,452,129	5,211,537	60,499	143,103	97,721	85,623	5,610,349	5,440,263	
Liabilities									
Financial liabilities - held for trading	-	-	83,128	32,988	-	-	83,128	32,988	
Derivatives	-	-	83,128	32,988	-	-	83,128	32,988	
Total liabilities	-	-	83,128	32,988	-	-	83,128	32,988	

Figure 3. Financial instruments measured at fair value in the statement of financial position

Source: https://cdn0.erstegroup.com/content/dam/ro/bcr/www_bcr_ro/EN/Investors/Financial-reports/2019/Financial_statements_June_30th_2019.pdf.

Financial assets held for trading increased during 2019, largely due to investments in bonds representing 91% of the total position.

Financial assets that are not held for trading and that are measured at fair value through profit or loss include:

Loans and advances granted to customers classified at fair value through profit or loss in accordance with IFRS 9 due failure to meet the conditions necessary to pass the SPPI test (excluding payment of principal and interest). Fair value calculation methodology of these assets correspond to the current base value technique in which the cash flows of the assets are discounted at full rate, including credit risk, market risk and cost components.

Credit risk is incorporated in the assessment of cash flows to reaches the expected cash flows, accounting for the customer's probability of default. These cash flows are then adjusted with discount rate.

Equity instruments, especially minority investments classified as level 3 instruments for which the fair value is determined on the basis of internal evaluation. Among the most common methods of valuing minority interests are:

- Quoted price on active markets,
- Expert opinion or recent trading value,
- Discounted cash flow method / dividend discount model,
- Adjusted net asset value,
- Simplified income approach.

Investments in VISA INC preference shares for which the fair value is calculated based on internal valuations and are classified by level 3.

Financial assets measured at fair value through other comprehensive income include:

Debt securities issued by the Ministry of Public Finance that are actively traded being classified as level 1 and 2.

A corporate bond having the theoretically established price, classified as level 3.

Valuation of level 3 financial assets

The volume of level 3 financial assets can be allocated in the following two categories:

The market values of derivative financial instruments when the credit rating adjustment (CVA) has a significant impact and is calculate based on unobservable parameters (internal estimates of PD and LGD);

Less liquid bonds, shares and funds that are not listed on an active market in which valuation models with parameters were used unobservable (e.g. credit margins) or broker quotes cannot be allocated to level 1 or 2.

The unobservable parameters in the CVA calculation are: the probability of default (PD ñ Probability of Default) and the loss in case of non-refund (LGD ñ Loss Given Default). Non-repayment probabilities are the result of internal estimates in the context of the development of rating models and are used in the assessment of credit risk, including CVA.

Each counterparty, depending on the rating received, is associated with a probability of default. The LGD parameter for the CVA calculation has the value of 60%.

As of December 31, 2019, the fair value of the preferred shares in VISA Inc. was based on reasonable assumptions and estimates and were classified on level 3.

The sale of shares is limited to certain conditions that may restrict the conversion of preferred shares into shares of VISA Inc. tradable.

Due to these restrictive conditions and to reflect the potential price volatility of VISA Inc. Class A common shares and the limited liquidity of the preferred shares, the fair value of the preferred shares was capped compared to the VISA common shares Class A Inc. based on assumptions.

The price of the Class C preferred shares was determined on the basis of the conversion ratio of 1: 13,952 and on the basis of two additional adjustment margins: a margin of 12.65% to take into account the uncertainty related to the market price taking into account low liquidity of class C shares; and a margin of 17.5% to reflect the risk of the conversion factor.

Figure 4. Movement of level 3 financial assets held at fair value:

Movements in Level 3 of financial instruments carried at fair value

						Group
in RON thousands		Gain/loss in profit or loss	Gain/loss in other comprehen sive income	Sales	Currency translation	
Assets	01.01.2019	-	-	-	-	30.06.2019
Financial assets - held for trading	2,133	55	-	-	-	2,188
Derivatives	2,133	55	-	-	-	2,188
Non-trading financial assets at fair value through profit or loss	36,995	(2,280)	-	-	-	34,715
Equity instruments	31,075	(575)	-	-	-	30,500
Loans and advances	5,920	(1,705)	-	-	-	4,215
Financial assets at fair value through other comprehensive income	46,738	-	14,785	-	-	61,523
Equity instruments	40,721	-	13,457	-	-	54,178
Debt securities	6,017	-	1,328	-	-	7,345
Total assets	85,866	(2,225)	14,785	-	-	98,426

						Group
in RON thousands		Gain/loss in profit or loss	Gain/loss in other comprehen sive income	Sales	Currency translation	
Assets	01.01.2018					30.06.2018
Financial assets - held for trading	2,875	(281)	-	-	-	2,594
Derivatives	2,875	(281)	-	-	-	2,594
Non-trading financial assets at fair value through profit or loss	39,118	2,060	-	(3,628)	10	37,560
Equity instruments	18,509	2,480	-	-	10	20,999
Loans and advances	20,609	(420)	-	(3,628)	-	16,561
Financial assets at fair value through other comprehensive income	33,846	-	6,748	-	-	40,594
Equity instruments	33,846	-	6,748	-	-	40,594
Total assets	75,839	1,779	6,748	(3,628)	10	80,748

Source: https://cdn0.erstegroup.com/content/dam/ro/bcr/www_bcr_ro/EN/Investors/Financial-reports/2019/Financial_statements_June_30th_2019.pdf

Figure 5. The table below shows the fair value of financial assets and liabilities at June 30th, 2019:

20. Fair value of financial assets and liabilities (continued)

20.1. Financial instruments whose fair value is disclosed in the notes (continued)

in RON thousands	Group					Bank					
	Carrying amount	Fair value	Fair value hierarchy			Carrying amount	Fair value	Fair value hierarchy			
			Level 1	Level 2	Level 3			Level 1	Level 2	Level 3	
											30.06.2019
Assets											
Cash and cash balances	10,346,352	10,346,352	10,346,352	-	-	10,179,024	10,179,024	10,179,024	-	-	
Financial assets at amortised cost	51,798,643	53,959,376	14,875,682	306,344	38,777,349	49,738,874	51,917,709	13,711,837	262,582	37,943,290	
Loans and advances to banks	269,108	271,236	-	-	271,236	280,364	282,492	-	-	282,492	
Loans and advances to customers	36,230,435	38,460,824	-	-	38,460,824	35,391,590	37,628,037	-	-	37,628,037	
Debt securities	15,299,100	15,227,316	14,875,682	306,344	45,290	14,066,921	14,007,180	13,711,837	262,582	32,761	
Finance lease receivables	1,062,774	1,062,680	-	-	1,062,680	3,241	3,241	-	-	3,241	
Trade and other receivables	493,065	515,924	-	-	515,924	477,790	500,706	-	-	500,706	
Liabilities											
Financial liabilities measured at amortised cost	61,890,320	61,646,348	-	279,822	61,366,526	58,881,083	58,647,643	-	279,822	58,367,821	
Deposits from banks	5,294,492	5,324,754	-	-	5,324,754	4,562,358	4,603,196	-	-	4,603,196	
Deposits from customers	55,427,344	55,142,904	-	-	55,142,904	53,150,871	52,866,384	-	-	52,866,384	
Debt securities in issue	269,613	279,822	-	279,822	-	269,613	279,822	-	279,822	-	
Other financial liabilities	898,871	898,868	-	-	898,868	898,241	898,241	-	-	898,241	

Source: https://cdn0.erstegroup.com/content/dam/ro/bcr/www_bcr_ro/EN/Investors/Financial-reports/2019/Financial_statements_June_30th_2019.pdf.

Figure 6. The table below shows the statement of cash flows at June 30th, 2019:

Source: https://cdn0.erstegroup.com/content/dam/ro/bcr/www_bcr_ro/EN/Investors/Financial-reports/2019/Financial_statements_June_30th_2019.pdf.

Statement of cash flows

in RON thousands	Group		Bank	
	30.06.2019	30.06.2018	30.06.2019	30.06.2018
Net result for the period	(20,843)	697,001	11,350	656,885
Non-cash adjustments for items in net profit/(loss) for the year				
Depreciation, amortisation of assets	125,444	91,778	100,637	64,231
Allocation to and release of impairment of loans	38,758	(39,935)	304,938	(50,443)
Gains/(losses) from the sale of tangible and intangible assets	20,602	(10,829)	18,105	(9,749)
Other provisions	601,350	(52,618)	280,071	(38,883)
Impairment tangible and intangible assets	13,220	(3,193)	-	7
Interest income received from investing activities	(332,240)	(328,289)	(309,479)	(299,839)
Interest expense paid for financing activities	(29,682)	82,006	(29,682)	75,068
Dividend income from investing activities	-	-	(13,464)	(7,953)
Other adjustments	(63,501)	(39,104)	(68,869)	(41,499)
Changes in assets and liabilities from operating activities after adjustment for non-cash components				
Financial assets - held for trading	81,743	(107,829)	81,743	(107,832)
Non-trading financial assets at fair value through profit or loss	-	25,847	-	25,869
Financial assets at fair value through other comprehensive income	(205,466)	-	(195,037)	-
Financial assets at amortised cost				
Loans and advances to banks	(145,268)	912,021	(169,470)	909,288
Loans and advances to customers	(1,430,879)	(1,530,728)	(1,310,610)	(1,395,383)
Other assets from operating activities	(68,855)	(6,918)	(36,947)	(46,146)
Financial liabilities - held for trading	-	514	-	514
Deposits from banks	(264,192)	(561,805)	(93,586)	(685,062)
Deposits from customers	328,385	(13,050)	557,181	113,625
Other financial liabilities	260,076	15,932	275,382	5,000
Other liabilities from operating activities	72,531	(12,893)	55,060	4,004
Cash flow from operating activities	(1,018,819)	(882,092)	(542,678)	(828,298)
Proceeds of disposal				
Financial assets - held to maturity	-	-	-	-
Financial assets at fair value through other comprehensive income	(727)	305,373	(727)	305,373
Property and equipment, intangible assets and investment properties	49,758	46,971	49,757	30,816
Acquisition of				
Financial assets - held to maturity	-	-	-	-
Debt securities at amortised cost	582,939	(564,412)	223,629	(519,862)
Financial assets at fair value through other comprehensive income	-	(5,835)	-	-
Property and equipment, intangible assets and investment properties	(177,990)	(140,395)	(66,538)	(55,570)
Contribution to increase in share capital of subsidiaries	-	-	-	(30,000)
Interest received from investing activities	332,223	679,425	309,479	630,067
Dividends received from investing activities	-	-	13,464	7,953
Cash flow from investing activities	786,203	321,127	529,065	368,776
Dividends paid to equity holders of the parent	(484,630)	(213,476)	(484,630)	(213,476)
Dividends paid to non-controlling interests	(466)	(14,587)	(466)	(14,587)
Debt securities issued	(91,061)	(90,661)	(91,061)	(90,661)
Inflows from other financing activities	364,106	326,277	-	-
Outflows from other financing activities	(285,525)	(816,169)	(56,917)	(641,284)
Interest expense paid for financing activities	(46,647)	(84,286)	(37,140)	(77,724)
Other financing activities	(23,033)	(32,300)	(13,526)	(25,746)
Subordinated loans	(23,614)	(51,978)	(23,614)	(51,978)
Cash flow from financing activities	(544,223)	(892,902)	(670,214)	(1,037,732)
Cash and cash equivalents at beginning of period	11,123,191	11,367,313	10,862,852	11,244,649
Cash flow from operating activities	(1,018,819)	(882,092)	(542,678)	(828,298)
Cash flow from investing activities	786,203	321,127	529,065	368,777
Cash flow from financing activities	(544,223)	(892,902)	(670,214)	(1,037,732)
Cash and cash equivalents at end of period	10,346,352	9,913,446	10,179,024	9,747,395

Real estate investments are systematically valued at fair value. Assets held for sale are valued at fair value when their carrying amount is depreciated below fair value less costs to sell.

The fair value of non-financial assets is determined by experts with relevant and recognized professional qualifications.

For non-financial assets held by the BCR Group, the valuation is made mainly using the comparative method and the investment method.

The assessment is made on the basis of the comparison and analysis of comparable investments and rental transactions, including information on demand in the area, in which the respective property is located. The characteristics of similar transactions are then applied to the asset to be valued, taking into account the size, location, contractual terms and other relevant factors. These valuations are presented in Level 3 of the fair value hierarchy.

For each reviewed stream of research, the paper establishes the theoretical underpinning and discusses its application supported by the context. The content analysis using NVivo software was employed to analyze existing research and available published information.

Earnings quality and the quality of accounting information are in direct relation. The usefulness of fair value information is explored directly by inspecting its predictive power with respect to future cash flows and future earnings..

They seek to anticipate the continuity of corporate earnings in the coming periods, while financial analysts point to financial statements as the primary source on which to analyze information and make rational decisions (Schipper and Vincent, 2003). For example, Barth., Beaver & Landsman, pointed out in 2001 that earnings are, of course, valued as indirect indicators for assessing the quality of accounting standards, as there is a direct relationship between the quality of earnings and the quality of accounting information.

There are different measures of income quality, the most well-known measures are persistence, predictability, quality of accumulations, income smoothing and relevance of value.

Predictability refers to the well-known fact that income is of higher quality and is more beneficial for predicting future income. It is noted that the predictive power of profits is affected by the time series of earnings and the fluctuation of business operations, the economic environment and the accounting system used by companies.

Sodan, in 2015, stated that the initial assumption of the value relevance of research at fair value is that fair value information predicts future cash flows. Therefore, instead of measuring the correlation between fair value estimates and market prices or returns, the usefulness of fair value information is, of course, examined directly by analyzing its predictive power in terms of future cash flows and future

revenues. Thus, fair value estimates are given by the present value of expected future cash flows, so if fair values are reliable measures of asset values, changes in fair values (i.e. unrealized gains and losses on fair value) should be reflected in future performance changes. (Barth, 1994).

Otherwise, if the fair value estimates are not reliable, then the correlation with future performance measures will not be taken into account. Among the most important accounting tasks is to choose the correct valuation method for valuing assets and liabilities.

This task has been shown by many scientists, such as McDonough & Shakespeare, 2015, who are determined that the financial position and results of economic activities represented in balance sheets and profit and loss statements depend not only on current reality but also on estimation methods. and calculation of reported indicators.

The concept of fair value emerged in the nineteenth and early twentieth centuries, but recently there has been much research and controversy among researchers calling for its cessation due to misuse and manipulation of accounting numbers at preparation of financial reports.

Abuse of fair value reached a peak during the twenties of the last century in many industrialized countries where prosperity and inflation have encouraged the development of optimistic repercussions of values, and many of them have returned to a significant decline due to the global recession (Thomason, 2017). Between 2006 and 2007, new accounting statements were issued that expanded the scope of fair value accounting, which led to a discussion that extended beyond the accounting profession to the rest of the business community.

Although fair value accounting is not a new concept or a new accounting practice, new data requirements coupled with the recent credit crunch that started in 2007 have caused many companies and users of financial data to question whether current fair value accounting practices should continue. Therefore, it is important to make a decision to resolve this difference because many companies that use fair value accounting have to record their assets and liabilities in difficult circumstances, such as the market crash, which makes the financial statements of these companies appear much worse than they really are. Since the purpose of financial statements is to clarify the financial condition of the company and its activities during the financial year and allow users of financial data to forecast future cash flows of the company, when the market collapses and the values of assets and liabilities appear below their actual value, this leads to distortion of the financial position of the company and it appears unable to achieve its intended goals (McDonough & Shakespeare, 2015).

In the retail banking activity, BCR granted new loans in local currency for individuals and micro-enterprises of over 7.8 billion lei (1.7 billion euros) in

2019, mainly due to mortgages, personal loans and those intended microenterprises. New loans for microenterprises increased by 31.5% in 2019 compared to the previous year, due to higher financing granted within the Start-Up Nation program. Unsecured loans increased by 3.4% compared to the previous year, due to the activity of personal loans and increasing the number of credit cards and overdrafts.

Regarding the corporate banking activity, BCR (bank only) approved new corporate loans amounting to 7.4 billion lei (1.6 billion) in 2019. The stock of financing granted to the SME sector (incl. BCR Leasing subsidiary) increased by 12.3% compared to past, reaching the value of 6.1 billion lei (1.3 billion euros) as of December 31, 2019, as a result of a higher concentration on new business and on the development of the leasing sector. The real estate segment increased significantly by 34.3% compared to last year, as a result of new office and commercial space construction projects funded in the last year.

The total number of customers increased to 3.3 million at the end of last year, compared to 3.1 million in 2018.

If the fair values of financial assets and financial liabilities recorded in the balance sheet cannot be obtained from the active markets, they are determined using a wide range of assessment techniques that include the use of mathematical models. The values entered in these models are taken from existing markets when possible, but when this is not possible, a certain type of reasoning is needed to set fair values. Presentations on valuation models, fair value hierarchy, fair value of financial instruments and analysis sensitivity for Level 3 financial instruments are described in Note 43 "Fair value of financial assets and liabilities".

The impairment loss model is a reasoning model because it requires the assessment of a significant increase in risk credit and measurement of expected credit losses without detailed instructions. Regarding the significant increase in credit risk, the group established specific evaluation rules consisting of qualitative information and quantitative thresholds.

Another area of complexity concerns establishing groups of similar assets when credit risk impairment must be assessed collectively before specific information is available individually.

Assessing expected credit losses involves complex models based on statistical data non-reimbursement probabilities and loss rates in case of non-payment, on extrapolation of information in case of insufficient observations, on estimates individuals of future cash flows and probabilities of different scenarios, including prospective information. In addition, the lifespan of instruments must be modeled in terms of the possibilities of early repayment and the behavior of credit facilities revolving.

Debt securities are measured at fair value through other comprehensive income (FVOCI) if their cash flows are compliant with the SPPI and are held within

a business model whose objective is achieved both by collecting contractual cash flows, as well as by selling assets. In the balance sheet, they are included as "Debt securities" under the line "Financial assets valued at fair value through other comprehensive income".

Interest income from these assets is calculated using the effective interest rate method and is included in the line "Net interest income" in the statement of profit or loss account. Impairment gains or losses are recognized in the income statement "Net impairment loss on financial instruments".

As a result, the impact of the recognized valuation in profit or loss is the same as for financial assets valued at amortized cost.

The difference between the fair value at which the assets are recognized in the balance sheet and the amortized cost component is recognized as accumulated OCI in equity, in the line "Fair value reserve" in the event of changes in equity. The change for that period is recorded as OCI in the statement of comprehensive income in the line "Debt instruments measured at fair value through other comprehensive income global".

Financial assets whose contractual cash flows are not considered SPPIs are automatically measured at fair value through profit or loss ("FVPL"). In the Group's activity, it refers to certain loans granted to clients, equity instruments and securities debt.

Another way of valuing the FVPL refers to the financial assets that are part of the residual business models, i.e. they are not even kept for the collection of contractual cash flows or not kept for the collection of flows or for their sale. In general, it is expected that these financial assets be sold before maturity or are valued from the perspective of business performance at fair value.

In the balance sheet, the debt instruments valued at FVPL are presented as "Financial assets held for trading", under the line "Other assets held for trading. "Financial assets are measured at fair value through profit or loss either because their cash flows contractual funds are not SPPIs, either because they are held as part of residual business models that are other than those held for trading.

In the situation of the profit or loss account, the effects produced by the financial assets valued at FVPL are divided into interest income or income from dividends and gains or losses on fair value. Dividend income related to equity instruments is presented in the line "Dividend income".

Fair value gains or losses are calculated excluding interest or dividend income and also include trading costs and issue fees. These are reported in the line "Net trading income" for assets financial assets held for trading and in the line "Gains / losses on financial instruments not intended for the measured trading mandatory at fair value through profit or loss "in the case of financial assets not intended for trading and are valued at FVPL.

Derivative financial instruments are used by the Group to manage exposures to interest rates, foreign currencies and other risks related to the market price. The derivative instruments used by the Group mainly include interest rate swaps, futures contracts, contracts forward, interest rate options, currency swaps and currency options, as well as credit risk swaps.

Derivative financial instruments are recorded at fair value (the price including the interest component) in the statement of financial position.

Derivatives are recorded as assets if their fair value is positive and as liabilities if their fair value is negative.

Derivatives held for trading are those that are not designated as hedging instruments against risks for hedge accounting. These are presented in the line "Derivative financial instruments" under the category "Financial assets / Financial liabilities held for trading". This item presents all types of derivative instruments that do not cover risks, regardless of their internal classification, both the derivatives held in the trading book and those held in the "banking book" portfolio.

Changes in the fair value (interest-free price) of derivative financial instruments held for trading are recorded in the profit or loss account in the position "Net trading income". Interest income / expenses related to both held for trading used for economic hedging, as well as hedging derivatives against risk are presented in the account profit or loss in the item "Other similar income" or "Other similar expenses" as "Net interest income".

The BCR Group continued to improve the ICAAP framework. It includes as its main pillar the ICAAP process (The internal evaluation process of capital adequacy to risks) required under Pillar 2 of the Basel Accord.

The ICAAP framework is a holistic risk management tool, designed to support the management of the BCR Group in the management of portfolios at risk as well as the potential for capital hedging, in order to ensure at all times the appropriate capital, able to reflect the nature and size of the Banks' risk portfolio and to support the business strategies and risk of these.

A key component of the ICAAP framework is the proper valuation of the Group's capital using economic capital measures. Within ICAAP,

The group identifies and measures risks and ensures that there is sufficient capital in relation to the risk profile. The process also ensures that they are used and develop appropriate risk management systems.

3. Conclusions

First, the paper concludes that the persistence, predictability, accruals quality, earnings smoothing and value relevance are the most important measures of earnings quality. Earnings quality and relation. The usefulness of fair value information is explored directly by inspecting its predictive power with respect to future cash flows and future earnings.

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