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Liquid Financial Means - Audit Aspects

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Abstract **Review Article**

The growing complexity of the business world, associated with economic and financial globalization, has led to an increase in economic activity between companies and countries, which has given rise to the need to adopt a set of internationally accepted accounting standards, in order to mitigate the different practices existing accounting records. This work is intended to explore the characteristics and context of class 1 Liquid Financial Resources, as well as the main impacts and audit procedures.
Keywords: Liquid Financial Means; Standardization System; Deposit control; Audit Tests.

1 - Net Financial Resources - accounting aspects

According to the Background Notes of the new Accounting Code created by CNC – Accounting Standardization Committee within the scope of the application of International Accounting Standards, Class 1 (Net Financial Resources) is intended to record all the net financial resources that include, either cash and bank deposits, or all financial assets and financial liabilities measured at fair value, whose changes are recognized in the income statement.

Included in this class are the accounts:

- Account 11 - Cash (cash in cash, such as bank notes and legal tender, national or foreign coins)
- Account 12 – Demand Deposits (financial means available in current accounts at financial institutions)
- Account 13 – Other Bank Deposits (financial means with specific characteristics that sometimes impose some limitation on their use, but which are easily convertible into known amounts of money such as time deposits and other deposits, namely, deposits with prior notice)
- Account 14 – Other Financial Instruments (financial instruments other than cash (account 11) or bank deposits that do not include derivatives (accounts 12 and 13) that are measured at fair value whose changes are recognized in the income statement)

Net Financial Resources are part of current assets. These are assets whose liquidity is immediate.

As a general rule, Liquid Financial Resources represent a small percentage of a company's assets, so materiality is low. However, the number of transactions carried out through the Net Financial Resources accounts is significant, compared to other accounts in the financial statements, so the inherent risk is relevant. Failure to pay its obligations on time can lead to the company becoming insolvent, even if it presents a positive result.

It should be noted that according to Almeida (2017):

1) Companies must have sufficient funds in order to meet their commitments in a timely manner. Otherwise your credibility may be affected;
2) The profitability of investments in Liquid Financial Resources, as a general rule, is low, which is why companies should avoid high volumes;
3) The treasury budget is a particularly important instrument, so that the company can anticipate inflows and outflows;
4) Movements in Liquid Financial Resources may reveal errors or frauds originating in other assets and liabilities

The main aspects of an accounting nature are as follows:

a) The cash balance should only consist of liquid means of payment. Thus, they should not be part of the cash balance, among others: cash vouchers, post-dated checks, fuel vouchers, meal vouchers;
b) Bank overdrafts must be recorded in a financing account under liabilities. Bank overdrafts are

unnatural balances (creditors) of demand deposit accounts

c) financial instruments [1] that are not measured at cost, or at amortized cost [2], should be measured at fair value [3]. If measured at fair value, transaction costs should not be included in the acquisition cost, being directly recorded in an income statement (NCR27 § 10);

d) Changes in fair value are recorded directly in results under losses on financial instruments or under gains on financial instruments (NCR27 § 11);

e) A transaction in foreign currency must be recorded, upon initial recognition in the functional currency, by applying to the foreign currency amount the exchange rate between the functional currency and the foreign currency at the date of the transaction (NCRF23 § 20);

f) At each balance sheet date: a) Monetary items in foreign currency must be translated using the closing rate; b) Non-monetary items that are measured in terms of historical cost in a foreign currency shall be translated using the exchange rate at the transaction date; c) Non-monetary items that are measured at fair value in a foreign currency must be translated using the exchange rates on the date the fair value was determined (NCRF § 22);

g) In the case of a financial instrument which, upon acquisition, incorporated interest in the acquisition price, this must be reflected in an account of other accounts receivable/payable.

2 - Net Financial Means - audit aspects

The auditor's role is to determine whether account balances exist, are legitimate and reasonable, are properly valued, accounted for, whether access to transactions is restricted, and whether the internal control system is appropriate and guarantees the safeguarding of assets.

Specifically (Almeida, 2017):

- The balances in the balance sheet correspond to the balances in the balance sheet;
- The opening balances are in line with the closing balances of the previous year;
- The amount recorded exists, that is, there is no lack of cash in cash and what is evidenced in current assets, namely, deposits corresponds to the responses obtained from financial institutions, within the scope of the circularization process. Thus, the cash balance shown in the balance sheet represents only the cash or equivalent liquid means of payment owned by the company. The balances of bank deposit accounts shown in the balance sheet effectively represent means of payment existing in credit institutions on behalf of the company. Account balances of negotiable securities and other treasury applications belong to the company. In case there are movement restrictions, they are properly disclosed in the annex;
- Balances are valued in accordance with what is required by the accounting regulations in force;
- They are only classified as active Liquid Financial Means that meet the conditions to be so;
- The annex contains all relevant information;
- Income and expenses are charged to the years in which they were generated;
- The amounts shown in Net Financial Means are appropriate to the type of business of the company;
- Internal control works and is tailored to the company's characteristics.

This is an area susceptible to various acts that can harm the company and lead to fraud situations. Situations such as misuse of collections (for example, misuse of checks sent by customers); appropriation of payments made by the company to its suppliers; obtaining payments through false justifications and embezzling money for personal purposes, among others, constitute evidence that justifies the existence of an effective and dissuasive internal control.

The audit work must be based on the survey of internal control. Based on this study, the auditor establishes the extent of the audit procedures and the timing of their application, in addition to making recommendations to those responsible for the deficiencies detected and their elimination.

Nabais (1993) states that the assessment of the internal control system is the basis that sets the nature

[1] According to NCRF27 “financial instrument: is a contract that gives rise to a financial asset in an entity and a financial liability or equity instrument in another entity”.

[2] According to NCRF27 "amortized cost of a financial asset or a financial liability: is the amount at which the financial asset or financial liability is measured on initial recognition, less capital repayments, plus or minus the cumulative amortization, using the effective interest method, of any difference between that initial amount and the amount at maturity, and less any reduction in impairment or uncollectibility"

[3] According to NCRF27 “fair value: is the amount for which an asset can be exchanged or a liability settled, between knowledgeable and willing parties, in a transaction in which there is no relationship between them. For the purposes of this standard, fair value is determined by reference to: a market value, in relation to financial instruments for which a reliable market can be easily identified; or when its market value cannot be reliably determined, the market value of components of financial instruments or a similar instrument; or to a value resulting from generally accepted models and valuation techniques, for financial instruments for which a reliable market cannot easily be identified,

and extent of the audit work procedures to be applied. If, after this evaluation, it is concluded that the system is operational and that the information collected is trustworthy, this tends to reduce the extent of the tests. If the assessment points to deficiencies in the internal control system, it is necessary to intensify the tests in aspects where weaknesses are found.

Almeida (2017) points out some characteristics that an internal control system in this area should highlight:

a) At the level of the company's structure:

a. There must be written rules on the functioning of the treasury department and its relationship with the other bodies of the company. The treasury must be separate;
b. The functions of each treasury employee must be segregated. Cash functions must be segregated from other operating operations and accounting operations. The segregation of duties has to do not only with employees from different bodies, but also with employees from the same body, but also with the fact that no employee should have the possibility of being responsible for an operation, from its inception to its term. The periodic rotation of employees from each agency among themselves is another way to achieve the same objective. It should be noted that segregation is not an absolute guarantee that fraud will not occur. For this purpose, collusion between employees is enough;
c. The custody of funds, payment functions, accounting and issuance and authorization of documents must be carried out by different persons. It is recommended to reduce the funds that are in the company to the essential minimum. They must also be placed in a safe place, properly protected and with restricted access;
d. Bank reconciliations must be carried out periodically. Bank reconciliation is the procedure that aims to ensure that a company's financial transactions are properly recorded in its accounts. It is about comparing the movements shown in the accounting with the movements registered by the banks. This reconciliation must be carried out by people other than those responsible for the teller and the banks;
e. Physical counts to the cashier must be provided for.

b) Payments by cashier:

a. There must be rules that determine the obligation for payments to be made by check or bank transfer when they exceed a certain limit. With the publication of Law No. 92/2017, of August 22, which approved the amendments to the General Tax Law and to the General Regime of Tax Violations, which entered into force on August 23, the prohibition of paying or receive cash, in transactions of any nature, carried out by natural persons residing in national territory involving amounts equal to or greater than EUR 3,000, increasing this limit to EUR 10,000 in the case of non-resident natural persons. Likewise, payments of invoices equal to or greater than 1,000 euros, or its equivalent in foreign currency, made by IRC taxpayers,;
b. It must be verified whether the documents justifying the payments that are in the box are original, are duly authorized and correspond to goods and services purchased by the company;
c. The amounts shown in the documents must be analytically proven in terms of quantities, discounts and taxes;
d. A fixed cash fund must be used. The fixed cash fund system consists of:
   i. Set an amount sufficient for cash requirements;
   ii. Deliver the aforementioned amount to the person responsible;
   iii. Verify the authenticity of the document that originates a payment and verify that it was duly approved;
   iv. Periodically update the fixed limit

Thus, the cash amount is limited and verification by an independent person is facilitated. At any time, the existing cash, plus the amounts corresponding to the documents paid must be equal to the fixed fund limit.

c) Cash receipts:

a. Receipts must normally be made by check or bank transfer;
b. Periodic reconciliations must be carried out between the collection records made in cash and by check, with the movements of the same funds in the bank;
c. The amounts received must be deposited with the financial institution. The full and immediate deposit prevents the accumulation of values and reduces irregularities;
d. Payments with amounts received must not be made.

d) Demand deposits:

a. Correspondence must be opened by an employee who does not have accounting or treasury functions;
b. The issuing of checks for payments must be the responsibility of an employee who will keep a copy of each check issued;
c. Blank checks must not be signed;
d. Payments must only be made for original documents and never for photocopies;
e. Checks must be registered, crossed and signed by two people whose functions are independent;
f. The signature of checks must be done in the presence of the respective supporting documents, previously verified, and the first person who signs must verify, initialing the agreement of the amount and the beneficiary. The second person must affix a "Paid" stamp;

g. If an existing check is cancelled, it must be filed after the signatures have been destroyed;
h. Checks outstanding for withdrawal for a long time must be canceled if no written contact is obtained from the beneficiary;
i. In the case of adopting the bank transfer modality, the precautions to be taken must be similar to payments through checks. The control is done through the analysis of bank reconciliations

The existence of effective internal controls tends to reduce substantive procedures. However, in the area of Liquid Financial Resources it is considered appropriate to carry out substantive procedures. As ISA 520 states "the auditor's substantive procedures at the assertion level may be tests of detail, substantive analytical procedures or a combination of both". The tests of details of transactions and balances are carried out in order to gather the necessary evidence to verify that the transactions and balances shown in the financial statements are correct. Analytical procedures are related to assessments of financial information through plausible relationships not only between financial and non-financial data.

In the case of detailed tests, the following are mentioned:

a) Cash count: this is the most important audit procedure to be carried out on the cash account and consists of a physical inspection, carried out by surprise, of the values in the cash register, which must always be carried out in the presence of the respective persons responsible;
b) Circularization of third parties: this audit test consists of confirmation with financial institutions of the balances presented in the respective accounts. In the letters signed by the responsible of the company and sent by the auditor, it must be requested that the answer be sent to the auditor. The letters must not contain any information about the balances shown in the accounts;
c) Analysis of bank reconciliations: The company must carry out periodic reconciliations. It is incumbent upon the auditor to verify the arithmetic accuracy, the proof through supporting documents of all the differences and the subsequent accounting of the differences detected;
d) Specialization of interest and valuation of financial instruments: the appropriate specialization of interest on deposits must be verified and whether the expenses and income of financial instruments measured at fair value were allocated to the year in which they originated.
e) Cutting of operations: it is convenient to check the movements carried out on the dates immediately before and after the end of the fiscal year.

In the case of analytical procedures, they do not, as a general rule, demonstrate a stable and predictive relationship over time. The balances of the Liquid Financial Resources accounts fluctuate quite frequently. However, the following procedures are recommended:

- Seeking justification for significant variations that have occurred;
- Obtaining explanations on the reasonableness of the balances, taking into account the cash needs and your indebtedness;
- Comparison of balances with forecast documents, namely, values from treasury budgets.

CONCLUSION

The study of Liquid Financial Resources is fundamental given that it is the area linked to the liquidity of companies. Auditing is essential to ensure its reliability and prevent fraud or deviations that could compromise the organization's operation. For future studies we intend to carry out a case study.

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