

Accounting basics - interpreting a trial balance

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Every business owner needs to understand an accounting balance sheet (*balanta de verificare*) in order to be aware of, in real time, the financial position of their company and the business decisions that impact it. The same applies to potential investors who are considering acquiring shares in a start-up or other companies, as they need to assess the risk of their investment.

The following briefly describes the basics of how to read and interpret the figures from a trial balance in order to determine,

- what expenses a company has
- whether it makes a profit or not
- whether it "yields" or requires capital, etc.

In Romanian accounting, classes 1 to 5 are balance sheet accounts that reflect assets and liabilities; classes 6 to 7, however, reflect expenses and income. As a rule, bookkeeping must always use the double-entry accounting method, i.e. every transaction in the bookkeeping is recorded in at least 2 accounts.

In the double-entry accounting system, total assets must correspond to the sum of total liabilities and total shareholder equity.

The trial balance therefore contains a lot of valuable information about the activity of a company, e.g. its type, employees, profit or loss. It is prepared monthly.

If the company carries out an activity, the corresponding revenue must be entered in account class 7 for current turnover. The scope of the activity can be seen from this and the number of accounts that record transactions.

The type of company, more precisely its field of activity (trade, production, services, etc.) can be identified by the same account class, which begins with the number 7. The main activity is generally assigned to the account with the highest turnover. Production companies have turnover recorded in account 701, trading companies in account 707 and service companies in account 704.

Whether the company pays corporation tax or micro-enterprise tax is determined by analyzing the expense account 691 for "Corporation tax expenses" and, inversely, account 441 - "Corporation tax" or account 698 - "Income tax expenses" and the inverse account 448 "Income tax".

To determine whether the company is making a profit or a loss, we look at the balance of the profit and loss account 121 (the last column on the right, the closing column). If the

balance of account 121 is in credit, the company is recording a profit. If, on the other hand, the balance is a debit, the company is recording a loss.

Account 117 - **Profit carried forward**, provides an overview of the result for the previous period. If there is a credit balance, the company has made profits in the previous financial years; if the balance is a debit, this means that the company has recorded losses. If this account has no balance, the profits from previous periods have been distributed (in the form of dividends) or the losses have been covered.

The company's fixed assets are derived from the class 2 accounts; they exist if these accounts appear in the trial balance and show a debit closing balance.

Items with a value greater than 2500 RON that a company acquires and uses over a longer period of time are considered fixed assets; their value is not considered an immediate expense, but is depreciated over their useful economic life. This value is therefore divided monthly into identical, smaller amounts and treated as an expense until the entire value of the asset has been depreciated over the statutory period. The depreciation accounts are also included in account class 2.

Other relevant information on the company is provided by account class 3 (inventories), debtor and creditor accounts (class 4) and cash and cash equivalents (class 5).

For newly founded companies, it is good to know that in the first year in which a profit is made, not all of it can be distributed as a dividend. Instead, a statutory reserve of 5% of the profit must be formed. The legal reserve must be continuously increased until it reaches 20% of the company's share capital.

Conclusion

Understanding the above figures is a prerequisite for determining the financial position of a company in real time and changing the corporate strategy if necessary. Of course, the premise for this is that the accounting is also managed accurately and professionally.

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