FINANCIAL - ACCOUNTING ASPECTS REGARDING THE ACCOUNTIN OF RISK COVERING TRANSACTIONS IN INTERNATIONAL COMMERCE

ASPECTE FINANCIAR - CONTABILE PRIVIND CONTABILITATEA TRANZACTIILOR DE ACOPERIRE A RISCURILOR IN COMERTUL INTERNATIONAL

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Abstract: *In Romania, the risk management activity is relatively underdeveloped. Risk is defined as being the exposure to a certain change or as the possibility of an adverse deviation from the forseen situation. Unforseen changes in the evolution of the interest rate, in the exchange rate or in the product price, not only affect the financial results of a company, but they can also cause its bankruptcy. The financial decisions are taken according to the cash-flows forseen by the future contracts, which are by excellence uncertain.*

Key words*: risk, forward transactions, futures and with options, hedging.*

INTRODUCTION

Different causes determine the international commerce operations, mainly the ones performed on commercial credit and in due time, to be exposed as they are being performed to a series of risks such as: the interest rate risk, the exchange rate risk, the risk concerning the price of comodities, the credit risk, the liquidity risk, the theft or catastrophe risk, competitive or strategic risks, the business cycle risk. Some of the protection measures have been and are still being taken by almost all participants, thus becoming common measures of the international commerce operations. In this regard we can exemplify the clearing of commodities through insuring payment ways and instruments, such as: the documentary letter of credit, the commerce effects accepted and approved by a bank, the insurance of commodities during transport etc.

The first measures of this kind were the transactions with execution at a certain term from closing of a contract, but at the price negociated upon by the parties upon the closing of the contract. These were called forward transactions.

ON TERM FORWARD TRANSACTIONS

The judicial basis of forward transactions is the forward contract, defined in the specialized literature as an agreement of will between two parties, the seller and the buyer, the first one to deliver, the other one to pay for a commodity or value at a certain future term (for example a currency) at a price established at the moment the contract was signed.

It appears that the following features are proper to forward transactions:

-the contract is made through direct negotiation between parties which agree upon: the quantity of commodity, its quality, the price, the delivery and the payment term of the commodity. It is not a typically bursary contract;

-the contract has a fixed value, the contract price being discounted at due date, regardless of the evolution of the market price. As a result, both the seller and the buyer can have favourable differences (profit) or unfavourable ones (losses) as a consequence of the transaction, according to the evolution of the market price compared to the contracted price.

-forward operations are physical commodity transactions, that is, at due date they are executed in kind: the delivery of the commodities or of the contracted value for the forward price;

-the execution of the obligations of the parties is guaranteed through the forward contract or through guarantees offered by the parties. The transaction is not guaranteed through a bursary mechanism like in the case of the futures operations and of the ones with options.

In practice one can encounter the following situations:

a.*The importer has an on-term debt in currency and makes a prevision of an increase of the level of the exchange rate.*

In order to ensure protection against currency risk, the importers can initiate forward operations by selling the national currency at the spot exchange rate and by buying the needed currency to cancel the debt at the forward exchange rate.

The position at currency risk is the currency debt towards the external provider. In order to cover the currency risk one must make a claim of the same size and with the same due date of the risk exposed debt. Simultaneously one must make an obligation to pay at due date the equivalent in RON of the currency at the forward exchange rate.

If the forward contract lasts as long as two financial exercises, then, at the end of exercise no. 401 ''Providers'' and 461 '' Various borrowers'' it is updated to the exchange rate of the last day of the year and the exchange rate differences are enlisted in the corresponding income accounts from exchange rate differences, that is expenses from exchange rate differences.

b.The exporter has an on-term currency claim and he forsees a decrease in the exchange rate.

For protection the exporters can initiate forward operations by selling currency (the collected currency from the contract) at the forward exchange rate and by buying national currency at the spot exchange rate.

The position exposed to the currency risk is the currency claim. In order to cover the currency risk one must make a claim in the national currency (account no.461 " Various borrowers'') of the same size and with the same due date as the commercial claim exposed to the currency risk and simultaneously an obligation (account no. 462 ''Various creditors") to pay at due date the equivalent in RON of the currency sold at the forward exchange rate. The difference between the two values, the forward exchange rate lower than the spot exchange rate is call forward contract discount, i.e. the currency is sold with a forward discount.

ON TERM FUTURES TRANSACTIONS

Like any transaction, the futures transaction is based on a contract. The contents of this contract is the commitment of the parties to delivery and to take over, at a future date (in a certain month), a commodity or a determined value, at price established at the moment of signing the contract, if at due date the position of the operator remains open. The one who assumes the obligation to take over the commodity (the buyer) opens a "long" position while the futures seller has a short position.

The definition of the futures contract mostly emphasizes its essential features, such as:

-the futures contract is a standard one from certain points of view: the nature of the basic asset (a certain quality of the commodity); the contractual quantity, that is, the transaction unit or lot (for example 10 tons of wheat); the execution term at which the close-out takes place.

It does not fit a certain calendar date- but a period of time-a month. The delivery months are pre-established and they quote at the stock exchange;

-the price of the futures contract is established within the stock exchange through the specific negociation and contract-signing procedure of this organized market.

According to the market conditions it varies daily and so the value of the contract is fluctuant by "market-marking'' of the prices. This makes it possible for the losses of one of the contracting parties to be transferred as incomes to the other party;

-the futures contract is executed by effective delivery (the delivery of the asset which lays at its basis) only by the operators whose positions remain open until the last transaction day stated in the contract. During the entire period from the closing of the contract until the execution term the short position partner (the seller) can cover his open position by buying something, and the one with a long position (the buyer) by selling something.

As an organized market, through which the price of the futures contracts is established, the contract workflow is ensured and the guarantee of executing the operations by the parties, the exchange implies specific transaction mechanism. In essence it refers to the following aspects:

-the transaction initiation, which is done by the operators (buyers-sellers) by the orders given to the broker companies with which they work for the closing of the contracts. At the same time the operators open special accounts at the broker companies in view of making the transactions. Initially the operators supply the deposit accounts with a margin-an established percentage, for example 10% of the value of the contracts.

Subsequently the level of the margin is updated, (through supply or flow) according to the updated value of the futures contracts through marking on the market. The gains or losses that come from the marking on the market of the contracts are discounted to the operators: for the gains they

obtain they collect liquidity in the deposit account, for the losses they have liquidity withdrawn from the account.

-the main role of the Clearing House in the functioning of the exchange through the fact that it ensures both the daily market - marking of the futures contracts and the assembly of the clearing, discount and delivery/receiving of titles operations.

In order to fulfill its attributions the Clearing House works directly with the brokers and the latter ones work directly with the operators (the buyers - the sellers) who do not know each other.

-the dissolution of the futures contracts on commodity can be done in two ways: by delivery, that is the giving/payment of the commodities or by closing-out the open position, that is by compensting it with an opposite sense operation.

The dissolution of the contracts by the effective delivery of the commodities, can be done, depending on the choice of the seller, in any of the working days of the delivery month as well as when his position remains open until the last transaction day stated in the contract, a case in which the Clearing House automaticlly disolves the contract. Remember though, that this manner of dissolution is rare in the asembly of the futures operations.

The close-out of the futures contracts by closing the open positions (clearing) is a rule of the futures transactions. In conclusion the futures transactions are not a way of effectively delivering the commodities that make the object of the contracts, but one initiated in order to benefit from the favourable price differences at exchange (speculative operations)

The second way of delivery also points out the fact that these operations can be and are initiated also from the desire of the operators to protect themselves against the risk for operations performed out of the exchange through the mechanism of the futures market. These risk-covering operations are known as hedging.

The accounting treatment of on-term futures transactions differs depending on the position of the operator for the commercial operation performed out of the exchange for which he wishes to cover the risk. From the point of view the accounting operations regarding hedging are divided into two categories: the selling hedging and the buying hedging.

a.The accounting operations regarding the selling hedging

The selling hedging is performed by an operator who, at a certain moment has in stock, buys or hopes to produce a quantity of physical comodity and at the same time or subsequently, sells an equivalent number of future contracts.

The transaction can also be presented as follows: if the price on the market decreases, which means a decrease in the value of the operator's physical commodity (loss), he makes gain from the futures contract, as he has a short position opened and the market has decreased (he sells or would sell and buys or would buy at a lower price).

b.The accounting operations regarding the buying hedging

The buying hedging is performed by the operator who intends to purchase a physical comodity at a subsequent date. In order to cover the risk of an increase in price he buys futures contracts at a present date. Having a long position when the futures price decreases he makes loss and when the futures price increases he makes gain out of the market-marking. In the end the transaction can have gain or loss as a consequence, according to the evolution of the market prices compared to his previsions.

ON-TERM OPTION TRANSACTIONS

An option is a negotiable-form contract closed between two parties, the seller and the buyer ,by which the seller of the option sells to its buyer the right to buy or sell an asset (comodity, currency or financial instrument) under certain circumstances (price, term of validity). It follows that, depending on their nature, option are of two types: call options and put options.

In their quality of derived financial instruments, options are characterized by the following features: the size of the option, the duration of the option, the exercise price, and the price of the option (the bounty). It is the price that the call or put buyer pays when he gets the option. It fluctuates and it depends on two elements:

a) the inherent value of the option, that is, the relation (difference) between the exercise price and the price of the basic asset in the case of call options, respectively between the price of the basic asset and the exercise price in the case of put options;

b) the value in time of the option, that is the additional value that exceeds the inherent one which the option can acquire on the market, as a result of the supply/demand of options.

Although the mechanism of option transactions is alike that of the futures transactions, still the nature of the value titles in options and the way in which the exchanges for options are organized gives it certain peculiarities:

-the initiation of an option transaction is made when the client opens an account at a broker company, where he deposits the entire option bounty (the price of the option). The deposited amount of money, made into a deposit, cannot be withdrawn from the account, as it serves for guaranteeing the transaction;

-the launching of the order of transaction of options through the broker company , after which, as a result of its execution at the exchange, the client acquires an option buyer or seller position;

The dissolution of an option contract can be performed in three ways:

a) by dissolving the option, during the period prior to the date the contract expires, through a transaction opposite to the initially acquired quality:

-the buyer of a call option sells the same call option in the exchange to another buyer;

-the buyer of a put option sells the same put option in the exchange to another buyer;

b) by exercising the option, that is, its acceptance by its owner followed by the delivery/receiving of the basic asset:

-in the case of the call option the seller chosen with the help of the exchange mechanism delivers the basic asset (the title) and the seller chosen with the aid of the exchange mechanism pays the exercise price;

c) by the expiration of the option, that is, its abandonment by the owner, a case in which it is cancelled from the inventory of the Clearing House.

The accounting treatment of on-term option transactions differs depending on the type of the option (call/put), on the direction of the performed operations (sale/purchase) and on the nature of the basic asset (commodity, currency or another financial instrument).

a. The call-option accounting operations

The buying option (call) gives the buyer of the option the right to buy from the seller of the option the basic asset at the exercise price established by contract, paying the option bounty for the realization of the transaction. At the same time the seller of the call option takes the

obligation to sell the basic asset to the buyer at the exercise price, if the option is exercised during the period of time established by contract.

If the price of the basic asset goes down below the exercise price, the call buyer makes loss, but the loss is restricted to the size of the bounty paid by giving up the right to exercise the option. The situation is vice-versa with the seller of the call option.

b. The put-option accounting operations

The selling/sale option (put) gives the buyer of the option the right to sell the basic asset to its seller of that option at the exercise price established by contract, paying the option bounty for the realization of the transaction. At the same time the seller of the put option takes the obligation to buy the basic asset from the buyer of the option at the exercise price, if the option is exercised during the period of time stated in the contract.

CONCLUSIONS

The on-term quotations within the currency sale/purchase operations are quotations which are valid at a date in the future-forward discount-established by the client, but calculated by the bank at present.

Such a product is useful for legal persons who perform exchange rate activities whose future financial fluctuations cannot be quantified with maximum precision due to the volatility of international and monetary internal exchange rate markets.

Particularly, the evolution of the EUR/RON exchange rate, as a result of the fluctuation on the international market of the EUR/USD exchange rate, has had negative effects upon the international activity performed by the Romanian companies.

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