ACCOUNTING APPROACHES REGARDING THE FACTORING BUSINESS

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Factoring is a modern technique of financing that is done especially in the countries which are developed from an economic point of view, the most important markets being the United States, Italy, Great Britain and Japan. In Romania, three- four years ago, factoring was a notion which was not too much utilized, but nowadays it tends to become a customary practice due to the needs of financing of the commercial societies.

This paper has as its goal a short presentation of the factoring operation and of the implications that these operations have upon the accounting of the factor but also of the adherent.

Key words: factoring, factor, factoring client, factoring debtor, cession of debts.

1. The description of the factoring operation

Factoring represents the operation of financing of the bills in order to rapidly get cash.At the basis of the factoring businesses there is the factoring contract, which is concluded between the adherent or the supplier, that owns a package of debts, and the factor, which in exchange for a commission which is received from the adherent takes on the obligation of paying the equivalent of the debts which are surrendered by the contract.

According to the criteria of classification, we distinguish the following types of factoring:

a) a) depending on the right of recourse that the bank can exercise upon the adherent, we distinguish:

- non recourse factoring – the factor pays the adherent the accepted equivalent of the bill, usually 80%, immediately after having been issued, and 20% in 180 days since the date of payment of the bill, even if it does not collect (totally or partially) one or more of the bills. In the interval of 180 days from the date of payment of the bill, the bank tries to recover the sums from the debtors or perhaps from the ensuring- reinsuring society to which it was ensured against the risk of non-collecting. The factor does not turn to the adherent in order to recover the equivalent of the bills, not having the right of recourse upon it.
- -recourse factoring – in the case of not paying, the factor will recover the sums which were not collected from the adherent, by exercising the recourse right, through the debiting of the current account of the adherent or through the capitalization of the security.

b) depending on the participants in the factoring operation, we distinguish:

- domestic factoring – at the basis of this operation there is an internal contract that takes place inside the same country and within it there is only one factor.
- international factoring – supposes the existence of an international commercial contract within which there intervene two factors (the import factor and the export factor). The export factor buys the debts of the exporter (also called the adherent) upon the importer, then surrendering them to the import factor.

The international factoring appeared as a consequence of the development of the national factoring, the important characteristics of the two forms being:

a) In the case of the national factoring, the undergoing of the contract supposes the participation of three parties:

- The supplier – it can render services or execute works, or a producer that delivers merchandise that according to the contract becomes a *factoring client* or an adherent.
- The beneficiary – it is the one that purchases the merchandise from the producer, benefits from the executed works or the rendered services and that according to the factoring contract will pay the bill directly to the factor. It is called a *factoring debtor.*

- The factor (usually a banking society) – buys the debts and finances the supplier. The factor, the supplier and the buyer undergo the transaction according to the national legislation of the country in which the operation takes place.It gets from the supplier a commission in exchange for which it pays the value of the package of surrendered debts, either totally, or partially in falling due instalments. The commission of the factor consists of agio and the security commission. Currently, in addition to these sums, the factor also holds back from the adherent the security of collection risk that is paid back to the adherent after the collection of the bills from the debtor clients. The factor performs the operation of financing in the local currency.

b) b) A contract of international factoring implies the participation of four parties:

- The supplier (exporter) – that delivers goods or renders services.
- The export factor (FE) – the one that performs the financing operation in the currency in which the exporter made the delivery of the good or the rendering of the service. This is exposed to the risk of exchange variations. We mention the fact that the supplier and the export factor are situated in the country of the exporter.
- The import factor (FI) – is responsible for the monitoring and the collecting of the funds from the importer.
- The buyer (the importer) – that purchases the delivered goods or the services which are rendered by the exporter.

The import factor and the buyer (the importer) are situated in the country of the importer. The export factor and the import factor collaborate on the basis of a code of rules regarding the international factoring.

2. Accounting aspects regarding the taking place of the factoring operation

The accounting treatment of the factoring operations will be different depending on the position of the factor in relation with the risk of cashing of the debt. As mentioned above, if the factor takes on the risk of cashing the debt, we speak of an operation of factoring without recourse (RPF), otherwise we speak of an operation of factoring with recourse.

In order to be able to discuss the accounting aspects of the factoring operation, it is necessary to clarify, according to the legal provisions and the current practice, who will do the bookkeeping and will present in the balance sheet the debts towards the factoring debtor.

a) In the case of the factoring contracts without recourse, the specialized literature considers that the factor has the right of property upon the debts which were taken over. By becoming the rightful owner of the debts which were taken over, the factor has the obligation of comprising them in the balance sheet.

The adherent (the factoring client) will eliminate from his bookkeeping the debts towards the factoring debtors, the debts which come from the delivery of goods or from the rendering of services. The factoring client will accentuate in his balance sheet only the debts towards the factor that will be maintained until they are settled by it.

In the accounting of the factor:

DEBIT (ACTIVE)		CREDIT (PASSIVE)
Debts which are bought towards the factoring debtors	=	Debts which are expressed in the buying price towards the factoring client(the sums which are paid in advance are subtracted)

In the accounting of the adherent (the factoring client):

DEBIT (ACTIVE)		CREDIT (PASSIVE)
Debts towards the factor to pay the selling price/ analytic factor (the sums which are paid in advance are subtracted)	=	

b) the case of the contracts of factoring with recourse is discussed in the specialized literature in a controversial manner. This is because there is still no concrete answer to the question: Who must keep the books and in whose balance sheet should it appear? Some specialists claim that the debts which are surrendered and taken over must be registered in the accounting and the balance sheet of the factor. Other groups of specialists uphold the theory according to which the lack of services of the factor leads to the marking out in the accounting of the adherent of the operations which are the object of the factoring. Because the opinions are divided and the normative acts of our country do not comprise exact and detailed provisions in this regard, it remains for the problem to be treated taking into account the specific character of each factoring contract.

The factoring operation presents accounting implications in the accounting of the factor, as well as in the accounting of the adherent. So we will take on the problem distinctly for each of the two parties which are involved.

The taking place of the factoring operation has the following succession: receiving the bills from the factoring client; separating the approved bills from the un-approved ones; financing the debts which come from approved bills; retaining the security of the risk of cashing; cashing the commissions; cashing the debt; giving back the security; cashing agio.

a) a) In the accounting of the factor:

The bills which are taken over by the factor are classified into two groups:

- bills which are approved, that generate the available term of factoring. These bills are available immediately under the form of credit in the account of the client, based on the presentation of some ensuring documents of the bank.
- bills which are unapproved or unavailable that generate the unavailable term of factoring. These bills are not approved until the cashing of the debts or until their contractual date of payment.

The factoring society can function from the point of view of the form of organization both as ***conventional societies of factoring*** (outside the banking societies) and as ***factoring societies that belong to banking societies.***

The conventional factoring societies will have to adapt the general plan of accounts which was approved by OMFP 1752/2005 modified through OMFP 2374/2007 to the specific of the factoring operation. In her book, which is called *The accounting of the operations of external commerce*, (Ed. Economică, Bucharest, 1997, p.224), Margareta Trașcă underlines an adaptation of the account plan to the operation of factoring. Keeping in view the changes which were brought to OMFP 1752/2005 modified through OMFP 2374/2007 the accounts which are utilized in the operation of factoring are the following:

- - the taking over of the debts from the adherent will be done utilizing the 2678 “Other immobilized debts” account and the 269 “Payments to be made for financial immobilizations” account.

The 2678 “Other immobilized debts” account will present three analytic accounts that will be utilized according to case:

2678.1 “Other immobilized debts/ available factoring”

2678.2 “Other immobilized debts/ unavailable factoring”

2678.3 “Other immobilized debts/ securities to the factoring operations”

The 269 “Payments to be made for financial immobilizations” account will be developed according to case:

269.1 “Payments to be made for financial immobilizations”/ approved bills

269.2 “Payments to be made for financial immobilizations”/ unavailable factoring.

I would like to mention the fact that there are on the market societies of accounting consulting that suggest for the financial brokering societies the use of other accounts than those which are presented above and namely:

4111 “Clients” – the nominal value of the debts which is taken over from the cessionary

401 “Suppliers” – with the value that is owed to the releaser of the debt.

- the management commission and the interest will be initially registered in the 472 “Incomes which are registered in advance/ factoring operations” account, going to be monthly marked out in the accounts from class 7. We are talking about accounts 766 “Incomes from interests”/ agio factor and 704 “Incomes from executed works and rendered services”/ commission factor.
- for the commission and the interest which is collected by the factor, the provisions of the Fiscal Code which was effective on the 1st of January, 2008, specify the compulsoriness of paying the Value Added Tax to the state budget, in a percentage of 19%, marked out in the 4427 “Collected Value Added Tax” account. The security will be taken in the 2678 “Other immobilized debts” account.

The factoring societies that function within the banking societies are usually the main societies that perform factoring operations. The plan of accounts which is specific to the banking societies, in accordance with Order no.5 from 22.12.2005 for the approval of the accounting Regulations which are in accordance with the European directives, which are applicable for the institutions of credit, modified and supplemented by Order no. 24/2006 and Order no.11/2007 provides special accounts for the taking place of the factoring operations. Thus we distinguish the accounts:

- at the signing of the contract the equivalent of the bills which are taken over from the adherent is registered outside the balance by using the accounts:

90319 “Other commitments in favour of the clientele” and 999 “The trade-off”

- the factoring debt implies the utilizing of the accounts:

20.112 “Factoring” – in which the nominal value of the mobilized debts and of the 25211 “Available factoring accounts” respectively 25212 “Unavailable factoring accounts” accounts is registered

- the management commission and the interest will be registered in the 70212 “Interests to the factoring operations” and 7029 “Commissions” income accounts
- the security for the risk of not cashing will be marked out in the 25336 “Other collateral deposits” account.
- the Added Value Tax which is afferent to the value of the commission and the interest will be marked out in the 35327 “Collected Added Value Tax” account.

b) in the accounting of the adherent (factoring client):

The general plan of accounts which is approved by OMFP 1752/2005 modified through OMFP 2374/2007 does not provide special accounts through which the adherent can mark out in accounting the taking place of a factoring operation. According to the specialized literature, in the accounting of the adherent there are two variants of bookkeeping of the operations of factoring:

1. The first variant (Vişan, “Accounting in external commerce”, Bucharest, 1999, p.82) supposes the taking place of the registering in accounting thus:

- the delivery of merchandise (and the issuing of the commerce bill with the specification that the beneficiary is really the factor, the commerce bill that is accepted by the importer not being given back to the drawer of the exporter but to the beneficiary):

4111” Clients/ Factoring debtor”	=	%	V
		707” Incomes from the sale of the merchandise”	
		708”Incomes from various activities”	
		766”Incomes from interests”	
		472” Incomes which are registered in advance”	

- the transfer of the debts of the factor, in order for it to pay the equivalent of the bills:

4111”Clients/ The factor” = 4111”Clients”/The importer V

- the cashing of the debts from the factor (the equivalent of the bills), excluding the value of the interest and of the commission:

5124” Accounts at banks in devices” = 4111” Clients” /The factor V-(C+D)

- registering the commission and the interest:

668 „ Other financial expenses” = 4111”Clients”/ The factor C+D

2. The second variant of reflecting in the accounting of the adherent (Margareta Traşcă – *The accounting of the operations of external commerce,* Ed. Economică, Bucharest, 1997, p. 224) presents itself like this:

– the debt which is accepted by the factor will be closed through account 2678 “Other immobilized debts” until the date of the collecting of the sums from the factor:

2678 “Other immobilized debts” = 4111 “Clients” / importer V

– cashing the debts from which the managing commissions and the interest held back by the factor are held back in the 622 “Expenses with the commissions” account, respectively 666 “Expenses regarding the interests” and Added Value Tax 19%.

%	=	2678”Other immobilized debts”	V
5124”Accounts at banks in devices”			Ci
622” Expenses with the commissions”			C
666” Expenses with the interest”			
4426”Deductible Added Value Tax”			D

– the value of the security which is held back by the factor will be registered in the 2678 “Other financial immobilizations” to a distinct analytic 2678.3 “Other immobilized debts/ securities to the factoring operations”.

5124 “Accounts at banks in devices”= 2678.3 “Other immobilized debts /securities to the factoring operations”.

Where : V – the nominal value of the approved bills ; Ci- the value which is cashed by the adherent; C- the value of the managing commissions; D- the interest

By analyzing the two variants we can state that the last variant would be preferred if we think that the external commerce society does not deliver merchandise to the factor but sells bills. Applying none of the two variants is not rigorously imposed but in practice the first variant is more utilized. We specify that for the registration of the income and the commission which are held back by the factor, according to the current legislation, it is recommended to use the 622 respectively 666 accounts.

In the end I would like to make some references to the cost of the factoring operations on the Romanian market. The collected cost for the factoring operations is divided into the tax for the managing of the transaction and a separate tax for the actual financing of the operation. Thus, there is a factoring commission and a financing one. The factoring commission is applied to the nominal value of the paid-for bills and represents 0.5-1% for the internal factoring services (in lei) and 1-2% for the export factoring services (in foreign currency).The financing commission is applied to the financed value, respectively to 80-90% of the equivalent of the bills, during the taking place of the contract. This is comparable to the interest which is applied to the short term loans (in lei or in foreign currency) and can be negotiated according to each transaction.

3. Conclusions

Factoring is an alternative to the classical models of financing, especially the operations of exterior commerce, that brings the clients the advantage of getting the financing in the shortest possible time, compared to the classical loan. It also allows the development of the business without immobilizing the actives of the societies in material securities, ensuring, at the same time, an efficient management of the debts. As we can see from the presentation of the paper, in the case of the banking societies, the bookkeeping of the factoring operations is ensured by registering into accounts which are especially provided for this operation. We cannot say the same about the accounting of the conventional societies of factoring (other than banking societies) and about that of the economic agents. The plan of accounts does not provide any special account for this type of operation, and the accounting legislation makes no concrete reference to the way of marking this out. If special accounts were introduced, each of the three parties which are involved could correctly and distinctly register in the bookkeeping the movement of the surrendered debts from every point of view. There are opinions of some specialists in this area, regarding the taking place of the factoring operations, to which I actually made a reference in this paper, but a legislative provision would clarify things, especially that during the last three, four years, the factoring operations in Romania increased.

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Factoring accounts receivable. Posted in: Accounting for accounts receivables (explanations). Definition and explanationÂ As the due date approaches, factor meets receivables and collects full amount of cash. The difference between the cash collected from receivables and the cash paid to the seller company forms the profit of the factor.Â When accounts receivable are factored without recourse, the factor (purchasing institution) bears the loss resulting from bad debts. For example, if a receivable whose account has been factored becomes bankrupt and the amount due from him cannot be collected, the factor will have to bear the loss. Journal entries: Under non-recourse factoring the seller makes the following journal entry The approach you use depends on various factors. Note that sometimes the approach to development of a new organization is essentially the same as the approach to development of its new product or service, particularly if the organization is new or only has one product or service. In that case, it might be difficult to detect any difference between the approaches to developing the overall organization and its new product or service.Â This approach is common to new businesses, especially if their founder is rather inexperienced in marketing analysis, and/or has a strong passion â€“ even an obsession â€“ about providing a certain product or service. He bases his belief almost entirely on his or her own perception, even though there is sometimes no verified evidence of a market for the product or service.