

**FINANCIAL AND TAX MANAGEMENT IN SMALL AND MEDIUM
SIZED INDUSTRIAL ENTERPRISES**

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Abstract

Target of this paper was to evaluate the importance of small and medium sized enterprises (SMEs) in Slovakia and to determine the application of financial and tax management in this type of enterprises. The results of our findings confirm that SMEs have an important role in Slovakia, and also that especially small businesses have little or no experience with the application of financial and tax management. Therefore the paper contains recommendations for financial and tax management of SMEs.

Key words

small and medium sized enterprises (SMEs), financial and tax management for small and medium sized industrial enterprises

Introduction

SMEs play an important role in the economy of countries with a developed private sector and competitive markets. They are considered to be the engine of economic growth and a major source of technological innovation and new products. They increase competitiveness and efficiency in markets and are often more flexible than large firms in adapting to new customer requirements, facilitating workforce change employment and play a major role in removing regional and sector imbalances in the economy

Materials and methodology of experiment

Our target was to assess the importance of SMEs in Slovakia, to check the application of financial and tax management in this type of enterprises and to suggest measures for their financial and tax management. Information has been obtained by processing of statistical data, solutions from final papers and interviews with managers of industrial enterprises.

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Reached results - Current status of SMEs and the application of financial and tax management in this type of enterprises

Definitions of small and medium sized enterprises vary from country to country. SMEs are mostly defined with help of quantitative measures (number of employees, revenues, owner's equity, etc.).

Slovakia has adopted the SME definition of the European Commission which, per recommendation 2003/361/EC, effective January 1, 2005, states that SMEs are autonomous enterprises which employ fewer than 250 persons, and which have either an annual turnover not exceeding 50 million euro, or an annual balance sheet total not exceeding 43 million euro. Within this category, small enterprises are defined as autonomous enterprises, which employ fewer than 50 persons and whose annual turnover or annual balance sheet total does not exceed 10 million euro. Micro enterprises are defined as autonomous enterprises, which employ fewer than 10 persons and whose annual turnover or annual balance sheet total does not exceed 2 million euro. All other enterprises belong to the group of large enterprises.

Development of enterprise structure by size category and by number of employees in Slovakia between 2009 -2011 is shown in the following figure (3).

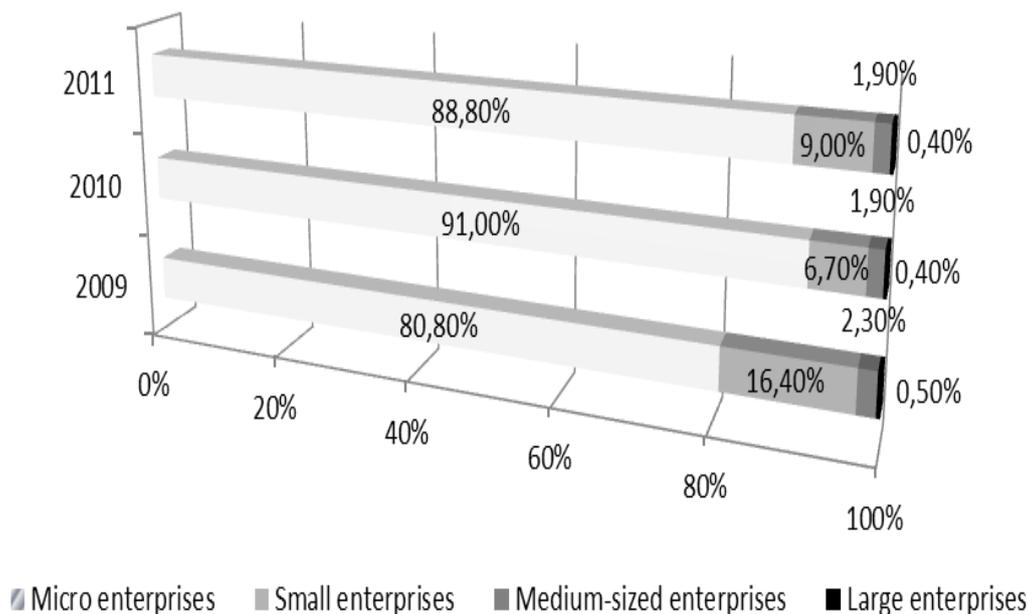


Fig. 1 Development of enterprise structure by size category

The importance of small and medium sized industrial and nonindustrial enterprises in Slovak economy is major. This fact is documented by the following numbers. Small and medium sized enterprises, including industrial enterprises, accounted for more than 42% of slovak imports, for 30% of exports, 42% of gross production, 56% of added value, 52% of profit before tax, for approximately 70% of total employment and for 99.6% of total number of enterprises in 2011 (Fig. 2), (3).

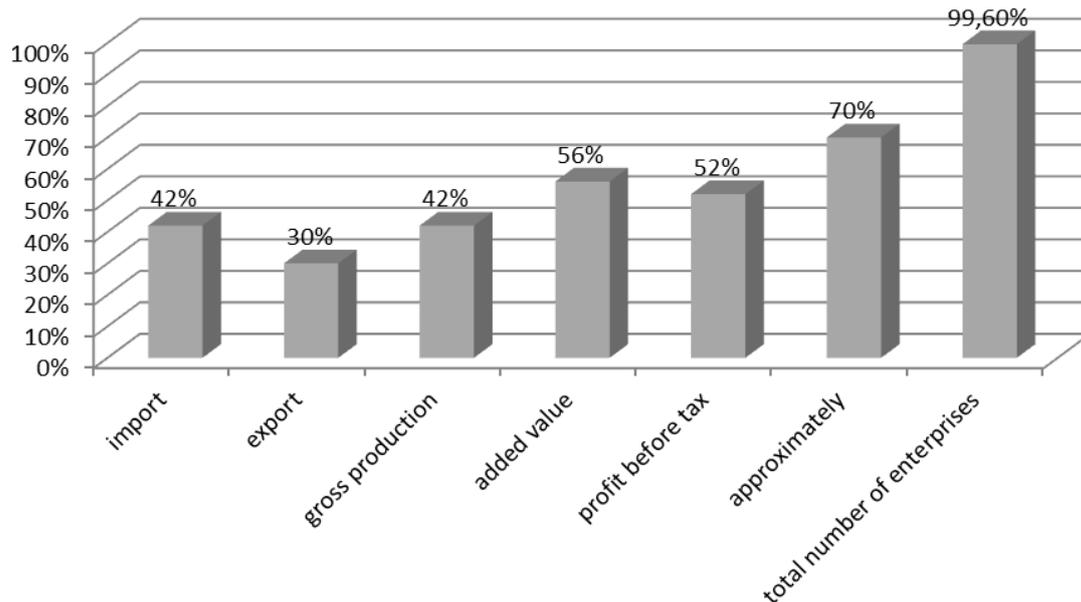


Fig. 2 *The importance of small and medium sized industrial and nonindustrial enterprises in Slovak Republic*

Most small and medium sized enterprises are active in services, in construction business and in industry. Industrial enterprises have an important role in the structure of SMEs. 16.3% of sole proprietors and 9.5% of small and medium sized partnerships and corporations were active in industry (3).

A key tool for helping SMEs survive in an ever-changing, highly competitive environment, is effective financial and tax management.

Financial management may be defined as a subsystem of overall company management focused on managing financial processes (financial planning, financial decision-making, organization of financial processes, and financial analysis and control), and with the goal of maximizing shareholder value. The main tasks of financial management are to obtain requisite financing, to allocate finances effectively, and to determine the company's profit sharing plan (1).

Taxes belong to unwanted, but from the law necessary costs of any enterprise. The logical effort of SMEs is to pay the lowest taxes and so maximize their net profit. This can be achieved by an efficient tax management, which is an integral part of the financial management. The tax management provides managing of financial processes from a tax perspective in order to optimize the tax burden of the enterprise. Tax management is one of the perspective directions how to improve the financial situation and competitiveness of small and medium-sized enterprises.

While financial a tax management is critical task for any size and type of company, it is especially critical for SMEs.

Based on our research, we found that the crisis had a negative impact on more than half of interviewed SMEs. Most companies felt this impact at the beginning of 2009. Over 50% of companies felt like the crisis had a major influence on their activities. They noticed significant decrease of revenues and limited access to external financing, especially credit financing. Some felt a pressure on price dropping, too. Lower return on investment caused problems with repayment of credit. Some companies became insolvent and had to use credit

to current account, or to increase owner's equity to solve this problem. It became more difficult for small companies to get bank approval of new credit. Only a limited number of SMEs were able to get financing through SZRB (Slovak guarantee and development bank), EXIM Bank, and micro-loan program.

Discussion - Measures in the area of financial and tax management of small and medium sized industrial enterprises

In the current economic literature, there is a debate on the best practices for companies' financial management in a global financial and economic crisis. Based on our research we have following recommendations for financial and tax management of Slovak SMEs:

1. During the crisis, it is important for SMEs to **reinforce long term planning** and to **create and implement appropriate corporate strategy and financial strategy** oriented to the primary company goal of maximizing shareholder value. Corporate strategy involves a company's choice of business, markets, and activities, and thus defines the overall scope and direction of the business. Financial strategy is one of several functional strategies. It supports corporate strategy and adds financial aspects to all strategic decisions. Financial strategy helps to evaluate the available operational alternatives, and helps to monitor the implemented decisions. Such valuation and monitoring of operating decisions is important for increasing expected cash flow for the company.

2. To be permanently ready to cope with financial and economic crisis, SMEs need to **monitor the economic environment** and recognize any warning signals of critical changes in their environment. Not only do they need to pay attention to the comments and estimates of various rating agencies and international banks, but also they need to analyze the financial health of their suppliers, distributors, and customers. Results of this monitoring need to be transformed into key variables for the planning process.

3. SMEs should also increase focus on **cash-flow management**. In order to survive the crisis, SMEs need to stay solvent and to have adequate liquidity. This can be achieved by intensive collection of receivables, reevaluation of business terms with suppliers and customers, monitoring of financial health of creditors and clients, management of working capital, and restructuring of debt.

Slovak government has taken various measures to help SMEs overcome the financial crisis. There are financial programs available to SMEs, which support innovations and technology transfer with the goal to achieve higher energy efficiency, to increase the effectivity of production, and to lower ecological impact. SMEs can apply for financial help through an operational program called "Competitiveness and Economic Growth," or through founding programs sponsored by the European Union; for example, the Competitiveness and Innovation Framework Program, or the Seventh Framework Program for Research and Technological Development (4).

4. Most SMEs use financial ratios to evaluate their firm's performance and its financial position. These ratios help to analyze current and past conditions, and are a starting point for future planning. In order to predict future development, it is necessary to monitor and analyze **non-financial indicators**; for example customer satisfaction, employee satisfaction, retention of high quality employees, and innovation grade. These indicators can help with the long-term prediction of company development by pointing to existing strengths, and to new opportunities for business.

5. For companies facing a decrease in sales, liquidity, access to credit, and are otherwise struggling to survive during the financial crisis, it is important to **analyze and limit costs**. This implies the elimination of unnecessary processes, which don't add to the produced value. At the same time, keeping the quality of products and services high is critical during the crisis. This factor may separate successful companies from troubled ones. The use of product norms, norms for quality management systems, and attitudes toward quality improvement are various ways of satisfying customer demands and enhancing the competitiveness of the enterprise (2). SMEs can also revise supplier agreements, negotiate pricing, payment and delivery conditions; can optimize storing of materials and products, lower their number of employees, better manage working capital, strictly control direct costs, reevaluate fixed costs, use outsourcing.

Small and medium companies are trying to optimize their tax liability and therefore it is necessary to implement tax management in financial management. Key functions of tax management is to tax planning, making tax decision and tax organization and tax control, which are interrelated and each of them includes a number of tasks.

From our perspective, the effective tax management in enterprises is important to ensure following activities: definition of tax policy in enterprise, monitoring of actual legislation, keeping tax records, executing tax reporting and internal tax analysis.

SMEs can't usually afford from financial and personal reasons to have a separate function of a tax manager, for the large companies is not a problem. In SMEs should be clearly defined issues of tax management and combined them with the tasks of financial management in a company that can perform e.g. financial manager, economist, accountant.

Conclusion

Indicators of Economic Development point to a growth in industrial production in the first half of 2012, especially in the production of vehicles. Slovakia has an open economy and therefore any fluctuations in foreign markets have an impact on our businesses. Small and medium sized enterprises are at greater risk and that's why they have to put emphasis on financial and tax management.

They need to implement a system of tools that will help them deal with current and future changes in business environment. We hope that our paper can be helpful in this process.

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