Straightening financial reporting

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First of two parts

Competing in the new competitive business landscape requires innovative solutions that enables a business to obtain a better snap shot of its business performance and standing. The increased necessity for a good financial reporting is driven not primarily by regulatory requirement. Rather, it is driven principally by increased demand for quality management reports. However, poor financial reporting oftentimes comes about due to corrupt practices, tax evasion and the traditional agency principal problems in the corporate world.

There are two general forms of poor financial reporting: (1) earnings manipulations; and (2) incomplete financial records. Poor financial reporting in the form of earnings manipulation pertains to various tweaks in the financial records of companies with a goal of either reporting overstated profit figures for better management reporting or understated profit figures to minimise, albeit, evade taxes. This form of poor financial reporting takes place primarily in corporate setting rather than for small businesses.

Poor financial reporting in the form of incomplete financial records pertains to incomplete recording of transactions by a company's bookkeeper or poor data (electronic and hard copy) retention practice rampant. This form of poor financial reporting usually applies to small businesses with bookkeeping outsourced to small practice firms or sole practitioners.

Businesses and owners often look outside of their business to understand market trends and data to analyse the economic insinuations. While analysing external information can provide significant insights on customer demands and market demographics, it is difficult to translate these information into a business specific information. What most businesses and owners fail to acknowledge is that the biggest source of their data is within their financial reports. Financial reports are expected to capture all financial transactions that occur throughout the life of the business and are composed of various transactions that can be used for analysis.

Recent years have driven many companies to appreciate the concept of big data and how they can leverage these massive data sets into useful corporate information. Removing poor financial reporting in the picture, data collected at a rock bottom granularity can provide significant insight into financial and non-financial information which could be significantly leveraged for business decisions. Notably, the practice of manipulating big data into insight have resulted to data science being a whole new business practice rather than being a purely academic topic.

The need for better information have proven to be a massively costly project for companies with long-standing businesses living without any financial records other than a blabber produced by their bookkeepers. These projects typically involve the reconstruction of the whole accounting records limited by the availability of back-up information and the consideration of various assumptions to compensate the lack of business records. Poor financial reporting resulting from earnings manipulation can be a real pain to discriminate fact from fiction. This would often entail the need for financial experts to help assess the extent of manipulation and cleanse the underlying data.

Straightening your financial reporting process from the very onset can provide substantial leverage on a company's long term strategy. In the short-run, the costs involved in setting up a good financial record can be burdensome. However, the long term benefit of having a good financial transaction history definitely outweighs the costs involve.

Filbert Tsai is a Filipino financial accounting advisory services executive in the UK with specialization in transaction accounting in the power and utilities sector. He had provided accounting advice to a significant number of government and financial institutions investing or providing financing structures in the renewables sector in Europe and in developing countries.

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