



Study on the Reform of the Current Financial Report System of China

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Abstract

In the times of knowledge economy, the financial environment of enterprises has changed largely, so the current financial report system of China has not satisfied the accounting information users' demand for the financial report. Three deficiencies existing in the current financial report system are analyzed in this article, i.e. lacking in the relativity, lacking in the timeliness, and lacking in the reliability. And corresponding reform directions have been proposed, such as using multiple measurement bases simultaneously, extending the scope of financial information disclosure and ensuring the information relativity, establishing the real time reporting system and ensuring the timeliness of information, and reducing the colors of the financial report and ensuring the reliability of information.

Keywords: Knowledge economy, Financial report, Reform

In the 21st century, the development of the economic globalization and the multi-directional development of the competition promote the world economy to enter into a new social economy form, i.e. the knowledge economy. Under the influences of the social economic form which basic characters include globalization, informationization, the networking and the knowledge-driven, the financial environment of enterprise has also changed largely. For example, the management environment of enterprise changes unendingly, and the production and operating activities of enterprise are more and more complex, and the fluctuation in price will be more frequent and drastic comparing with past, and the industrial competition is more and more drastic, which make the uncertainty of the enterprise management is higher and higher. Therefore, the current financial report system of China has not satisfied the accounting information users' demand for the financial report. Though the current financial report system follows the special accounting rule and adopts the standard and current format of presentation, but with the advent of the knowledge economic times, its advantages such as synthesis and standardization have not remedied the deficiencies shown because of the lagging behind the change of the economic environment. The current financial report system urgently needs a profoundly reform oriented by accounting information users' demand. The deficiencies existing in the current financial report system under the new social economy form are analyzed in this article, and advices are provided for the reform direction of the financial accounting report system of China.

1. Deficiencies existing in the current financial report system of China

1.1 Lacking in relativity

The information offered by the current financial report mainly includes the historical information facing to the past, and the financial report is basically a historical accounting data sheet, but the users of the financial report hope to reflect the future performance and financial status of the enterprise, especially the cash flow forecasting information which has important reference value for users' future decisions. So this financial report mode which is established in the happened certain trades and affairs require lower information relativity for users' decisions. The historical cost financial report lacks in forecasting information, which can not provide useful information for information users' decisions and send a warning signal, but sometimes may mislead investors and judge the mistakes. For example, in 1980s, about 2000 financial corporations which engaged in the financial instrument exchange in US were misled because of the "good" management performances of their financial reports in the crisis, and found themselves in the financial trouble. Therefore, people gradually realize that the traditional income table which takes the historical cost as the econometric mode lacks in the relativity, and can not satisfied the demand for the forward-looking information.

In addition, the information disclosure range of the current financial report has not satisfied different information users' demand for the information relativity. With the quick development of social economy, many different accounting information users including investors, creditors, government branches, partners, social sectors occur in and out of enterprises. These accounting information users need not only the financial information, but also the non-financial information, need not only the quantitative information, but also the qualitative information, need not only the certain information, but also the uncertain information, need not only the historical information, but also the forecasting information, need not only the total information, but also the part information. The current financial report can not satisfied their demand for the information, so the relativity of the accounting information has been weakened.

1.2 Lacking in timeliness

Managers hope to obtain required accounting information at any time in the decision-making process, but the annual financial report of the enterprise is made in the late four months of the year, and the interim financial report needs to be made in the last two months when the interim term ends. So the disclosure requirement of the current financial report can not achieve the timelessness of the accounting information quality. The traditional accounting tradition requires that the annual disclosure accounting information should be based on users' demands for the annual wealth distribution and the information disclosure cost in the manual accounting, but this financial report based on the time-period concept periodic planning has obviously hysteretic nature, which seriously influences the timelessness of information, even makes the enterprise to lose the commercial chance. The Barings Bank of the British is a classical example. In the late of 1994, the book net value of the Barings Bank was 45 billion to 50 billion dollars, but after two months, i.e. in the late of the Feb of 1995, the financial status of this bank had changed largely, and the bank had entered into the bankruptcy, and at that time, the financial report of 1994 had not be completed. It is obvious that the disclosure requirements of the current financial report have not accorded with the requirements of the development of the modern society.

1.3 Lacking in reliability

The information provided by the current financial report may be influenced by the accounting personnel's subjective factor, and lack in the reliability. To reasonably reflect the key business ratios, report the financial statuses of enterprise, and the management result and the cash flow, accounting personnel would implement large numerous of adjustments and transfer accounts according to the matching principle at the late of the term. Though accounting personnel implement the accounting confirmation and measurement for the financial data based on the actual trading items, but these transfer accounts and the matching processing have certain subjectivity, and the financial report of the enterprise provides the accounting information for the exterior benefit relation group including investors and debtors, and the management layer and the accounting personnel of the enterprise all hope that the financial report could reflect good financial status and the management result of the enterprise, so the accounting personnel may make the financial report with colors when they make the financial report.

2. Reform directions of the current financial report system of China

Aiming at the deficiencies existing in the current financial report of China, following opinions are provided for the reform.

2.1 Using multiple measurement bases simultaneously to make information with more relativity

When selecting the econometric base of the financial report, American Accounting Association, the Institute of Chartered Accountants in England and Wales and the Institute of Chartered Accountants of Scotland all took the relativity as the first standard. American Accounting Association thought that "when selecting the econometric base of the financial report, we will firstly consider the relativity. Though the reliability of the data is important, but the reliability of irrelevant data is useless for anyone." And the Institute of Chartered Accountants in England and Wales and the Institute of Chartered Accountants of Scotland also pointed out that "to reflect their own characters, the assets and liabilities will adopt the compromise solution to compute the price" in "the Mode of Future Financial Report" published in 1991. Therefore, the reform direction of the future financial report is using multiple measurement bases simultaneously, i.e. different assets and liabilities adopt different econometric bases to make information with more relativity. The concrete measure is to first divide the accounting information disclosed by the financial report into the core information and the non-core information, and then to adopt the historical cost with strong reliability as the econometric base to disclose the core information, but for the non-core information, to adopt the similar prevailing market price which reliability is not as good as the econometric base of the historical cost to disclose it.

2.2 Extending the scope of the information disclosure to make information with more relativity

2.2.1 Continue to perfect three basic financial reports

The current financial report system is the mono layer report mode taking three basic financial reports including the asset balance sheet, the profit statement and the cash flow statement as the core. This mode should be developed to the higher level and deeper layer. Future financial report system should start from the accounting information users' actual demand, and provide a series of relative financial information needed by the development in the modern market economy and the competition with other same industrial enterprises for them. First, some items in the asset balance sheet and the profit statement should be concreted according to information users' actual demand, and the range of the information disclosure should be extended. Second, some items in the asset balance sheet such as the stock, receivables, and market values have large influences, so the current market value can be a corresponding complementation form listing in the asset balance sheet to make information with more relativity.

2.2.2 Enrich and standardize the content of the information disclosure out of the financial report

With the increasing complexity of the economic activities of the enterprise and the increasing enhancement of

accounting information users' requirement for relative information, and the function of the outside form information (including the annotations of the financial report and other financial reports) for users to correctly understand the data of the financial report and judge the quality of the financial report increase increasingly, so to gradually extend the range of the information disclosure can satisfy report users' demand for useful information.

(1) The information of knowledge capital should be fully disclosed.

The information of knowledge capital mainly includes the intangible assets of enterprise, human capital information, and the human resource information. The intangible assets of enterprise include the intellectual property possessed by the enterprise, the vanguard technology or goodwill. If these intangible assets can not be exactly listed in the report, relative information should be disclosed by other modes. The values of the human resource and the human capital can not be embodied in the current financial report, and in spite of how large the disbursements investing in the human resource, they should be all regarded as the period charges, which will induce that the total assets are underestimated, and the charges are overestimated, and accordingly laborers' economic contributions to the enterprise are underestimated. Therefore, in the future financial report, the disclosure of the knowledge capital information should be emphasized.

(2) The comprehensive income information of the enterprise should be fully disclosed.

The comprehensive income of enterprise means the increase or the decrease of the rights and benefits (net assets) induced by all causes except for the trades with the owners (such as the investors' investment and the distribution of dividend) in the report term. So the comprehensive income includes not only the net yields which have been realized and confirmed in the current profit sheet, but other benefits and losses which have not been realized, such as the unconsummated surplus charge property reappraisal and the unconsummated return and loss on investment. The current financial report follows the realization principle for the confirmation of the accounting income, so the current profit sheet doesn't confirm the unconsummated income, so the comprehensive income of the enterprise in the term can not be reported according to the facts. This method makes the income computation to lack in the coherence of logic, which brings a certain space for the enterprise to manipulate the profit or color the performance. For example, it is a usual profit manipulation method to turn the unconsummated profit or loss to the current profit and loss by the replacement of assets. Therefore, in the future financial report, the disclosure of the comprehensive income information of the enterprise can be emphasized.

(3) The contribution of enterprise to the society and the distribution information of the contribution amount should be fully disclosed.

The contents disclosed by the current financial report mainly include the information about the investors and debtors' investments, the profitability and the financial position about the credit decision, but the contribution of enterprise to the society and the distribution information of the contribution amount can not be reflected. In the day that the politics and economy are more and more democratic, the method of the current financial report can not satisfy the demand of the society for supervising the enterprise implementation, and make against the country to implement the macro-control. Therefore, in the future financial report, the added value statement can be regarded as the fourth accounting statement after the succeeding asset balance sheet, the profit sheet and the cash flow sheet, and the by the added value statement, the contribution of the enterprise for the society can be comprehensively measured.

(4) The forecasting information of the future value of the enterprise should be fully disclosed.

The current financial report can not offer the forecasting information of the future value tendency of the enterprise for users, but the investors and potential investors of the enterprise need more and more grasp the future management development of the enterprise when the capital market of China is gradually perfected. But these report users can not reasonably predict the future development status of the enterprise because they can not know their experiences, technologies and enterprises enough. Therefore, the future financial report should disclose the relative information about forecasting the future value tendency of the enterprise in detail as more as possible, such as the profit prediction of enterprise, the increase or decrease of material cost, the development of new products, and the far-seeing plane of the management authority.

(5) The profit and risk information induced by the derivative financial instruments should be fully disclosed.

In recent years, the derivative financial instruments are more and more, and they will largely influence the future financial state and the profitability of the enterprise, but the current financial report can not disclose the relative risks. This method may be likely to produce potential risk for the accounting information users, and induce their decision mistakes in the investment and credit. Therefore, the future financial report should emphasize disclosing the profit and risk information induced by the derivative financial instruments.

(6) The stockholders' equity dilution information should be fully disclosed.

The development of the securities market induces that the stockholders' economic benefits more come from the market

price different of stock, not only in the profit of the enterprise. So stockholders very care about the market value of the stock. Because the book value of the stock is often lower than the market value of the stock, so when the company issues the convertible bond, the bond interest can be reduced by reducing the convertible price, and the interest charge reduced by the decrease of the interest rate will be turned to the profit of the enterprise, which will increase the profit of the enterprise. This profit increase is based on the stockholders' equity dilution, but the current financial report can only reflect the increased profit, but the accounting of original stockholders' equity dilution is eliminated. This method will certainly induce that investors falsely judge the behavior that the company issues the convertible bond, and make the false decisions. Therefore, the future financial report should fully disclose the stockholders' equity dilution information.

2.3 Establishing the real time report system to make information with more timeliness

The development of the modern network information technology provides the possibility that the enterprise publicly discloses the real-time financial information. The "real-time" includes the absolute "real-time" and relative "real-time". The absolute "real-time" report means that the enterprise reports one when one trade happens according the cost benefit principle and the situation of the enterprise. And the relative "real-time" report means that the enterprise can report in one day, in ten days, in half month, or in one month. The real-time report system can effectively solve the time-efficiency of financial information, and it can provide useful multi-directional financial information to make decisions for investors, and help management decision-makers and information users to make right judgment, and make their decisions more face to the future. However, the establishment of the comprehensive real-time report system needs strong internet technology support and a perfect ERP system. By the layer-upon-layer authorization mode of internet interview, the comprehensive real-time report can make some accounting information to occur by the mode of "private goods", which can solve the problem that the accounting report cost can not be reasonably apportioned. The online real-time report can also offer the hardware support for information demander to actively participate and realize the report of "cutting the coast according to the cloth", and realize the "interaction" of the report. In addition, the report users can interview the database of the enterprise of the Internet, and acquire the information that the enterprise issued on the internet, so the printing and the transfer mode of the paper financial report will be gradually eliminated. The expression modes of the information issuance on the internet can adopt the figure and video to more visually express the information and make the information more easily to be understood and accepted by users. Therefore, enterprises should establish and gradually perfect the ERP system, and try to realize the successful and reasonable connection with the Internet, which can build the base for the establishment of the comprehensive real-time system and solve the problem of the lagged financial information.

2.4 Reduce the color of the financial report to make information with more reliability

2.4.1 Perfect the enterprise governance structure and reduce the coloring condition of the financial report

First, the enterprise financial report users' motivation and ability participating in the supervision should be strengthened. Second, the interior supervision mechanism of the enterprise should be perfected. By these measures, the financial report users can more deeply understand the behaviors of the management layer, enhance their ability of information collection and judgment, and increase some supervision measures for them.

2.4.2 Perfect the performance evaluation mechanism and the manage personnel salary system, and reduce the coloring motivation of the financial report

At present, the evaluation for the managers of the enterprise should be based on the financial index of this enterprise, so some managers would rather color the enterprise financial report to acquire larger performance and obtain higher salary in more risks. To solve this problem, the enterprise should modify the current performance evaluation method, i.e. the enterprise should comprehensively consider numerous factors such as the leadership, the strategic planning, the management performance and the human resource management when evaluating the performance. By perfecting the performance evaluation mechanisms and the management personnel salary system, the coloring motivation of the financial report can be reduced.

2.4.3 Perfect the CPA system and exert the function of preventing the coloring of the financial report

The independence of CPA auditing should be firstly strengthened, and the licensed environment should be optimized to make the CPA auditing to be independent substantively. Finally, the relative departments of the government should supervise the CPA auditing to enhance the auditing quality and prevent the coloring behaviors of the financial report.

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