CSCanada
International Business and Management
Vol. 10, No. 2, 2015, pp. 28-31
DOI:10.3968/6617

ISSN 1923-841X [Print]
ISSN 1923-8428 [Online]
www.cscanada.net
www.cscanada.org

Improving Consolidated Financial Statement Working Papers and Normalizing Preparation Process

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Received 22 January 2015; accepted 9 March 2015
Published online 30 April 2015

Abstract

Preparation for the consolidated financial statements plays an important role in business merger. This paper analyzes the preparation process and formats of consolidated financial statements working papers in China Certified Public Accountant (CPA) materials in recent years. Based on our studies, we propose improved formats of consolidated financial statement working papers and normalized preparation process.

Key words: Consolidated financial statement, Working papers, Optimization statement

Li, L., & Wu, J. M. (2015). Improving Consolidated Financial Statement Working Papers and Normalizing Preparation Process. *International Business and Management, 10*(2), 28-31. Available from: http://www.cscanada.net/index.php/ibm/article/view/6617
DOI: http://dx.doi.org/10.3968/6617

INTRODUCTION

Preparation for consolidated financial statements is complicated. The working papers formats and preparation process are evolving in current CPA materials, however, there are still problems such as enormous calculations, confusing format framework, and hardness. As a result an understandable but powerful working papers format is needed to prepare for consolidated financial statement. This paper first summarizes the current trends of consolidated financial statement preparation process in popular CPA materials. We then propose improved consolidated financial statement preparation process to explicitly reflect the parent-subsidiary merger based on our studies. By combining scientific and practical methods, our work helps the users to better understand the financial statements as well as to avoid forged financial statements made by holding companies for profit manipulation.

1. IMPROVING CONSOLIDATED WORKING PAPERS

1.1 Existing Format of Working Papers

There are various types of working papers formats in existing materials. Our work is based on the most popular formats in CPA materials.

As shown in Table 1, the adjusting entries are internal within each parent and subsidiary in the 2010 consolidated financial statement working papers. But the users only need the subtotal after merger. Thus the internal adjusting entries are meaningless and increase the workload.

The 2011 consolidated working papers shown in Table 2 are similar to the 2010 working papers. The internal adjusting entries are eliminated. But it is still tedious to list the debit and credit amounts for each internal statement since the users only need the totals (total amounts) in the working papers. The users only need to identify which amount items to adjust, not need to distinguish which individual data in certain member company. So these adjusting entries formats in consolidated working papers are to be modified.

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Table 1
Consolidated Working Papers (2010)

Items	Parent			Subsidiary1			…	Subtotal	Offsetting entries		Minority interests	Subtotal
	Amount	Adjusting entries		Amount	Adjusting entries				Debit	Credit		
		Debit	Credit		Debit	Credit						
(Income)												
…												
(Changes in equity)												
…												
(Balance)												
…												
(Cash flow)												
…												

Table 2
Consolidated Working Papers (2011)

Item	Parent			Subsidiary1			…	Subtotal	Offsetting entries		Minority interests	Subtotal
	Amount	Debit	Credit	Amount	Debit	Credit			Debit	Credit		
(Income)												
…												
(Changes in equity)												
…												
(Balance)												
…												
(Cash flow)												
…												

Table 3
Consolidated Working Papers (2012-2014)

Item	Parent	Subsidiary1	…	Subtotal	Offsetting entries		Minority interests	Subtotal
					Debit	Credit		
(Income)								
…								
(Changes in equity)								
…								
(Balance)								
…								
(Cash flow)								
…								

In Table 3, the format of consolidated working papers stays the same from 2012 to 2014. Also, compared with that in 2010 and 2011, it deletes the internal adjusting entries in each of the reports, which simplifies the format. However, the totals among all the reports is not just adding up the internal numbers. Instead, the summation is an adjustment. As a result, the lack of these totals in these kinds of working papers will mislead the expected users.

1.2 Improving the Formats of the Working Papers

Via the above analysis, we summarize the suggestions to improve the working papers in Table 4.

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Table 4
Consolidated Working Papers

Items	Parent Amount	Subsidiary11 Amount	…	Adjusting entries		Subtotal	Offsetting entries		Minority interests	Subtotal
				Debit	Credit		Debit	Credit		
(Income)										
…										
(Changes in equity)										
…										
(Balance)										
…										
(Cash flow)										
…										

The advantages are summarized as follows:

(1) Compared with the format in 2010, no adjusting entries are set in the consolidated financial statement, and it can simplify the format of working papers.

(2) Compared with the format in 2011, after adjusting entries, the suggested format proposed here set the column to record the total number. It will help to enhance how to get the total number through offsetting

(3) Compared with the format in 2014 (same with 2012 and 2014), adding the internal modification entries, it will clearly show the modification processes of parent companies.

2. THE STANDARD FOR THE COMBINATION OF FINANCIAL STATEMENT PROGRAMS

2.1 Preparing a Piece of Blank Working Paper

Currently, almost all of the materials regard this step as consolidating working papers. More accurately, this step can be seen as making the preparation of blank working papers. This step is used to make preparations for the combination of the financial statement. Also, here it should process or modify the cost for different programs in the parent and the corresponding subsidiary companies, and finally it will calculate the number of different programs in the consolidation of financial statement. So far, there have not been uniform format for the work draft. In this paper, we make up all the formats in the materials of CPA examinations in recent years, which are shown in the Table 1.

2.2 Putting Data in Some Financial Statement into the Consolidated Working Papers

In this step, we need to take profits and loss reports, owner's right change reports, debts reports, and cash flow reports in the parent and corresponding subsidiary companies into the consolidated working papers.

In the materials of CPA examinations from 2012 to 2014, we calculate the total number of the data in the working papers. This is because the data in each of the reports are meaningless, and what's more, they will cost more to consolidate financial statements.

2.3 Adjusting Entries

Before consolidating financial statements for the subsidiary companies that are got from companies' consolidation under different control, it should check out the debts reports for the subsidiary companies based on the original parent companies.

Through modifying the entries, modification for the financial statements from the subsidiary companies will make up-to-date identified property and debts clear. For the subsidiary companies that have different financial policies and periods from the parent companies, if the parent companies had ever modified some financial report, it also should modify the entries during consolidating working papers. To make the consolidated working papers, it should change the long-term stock right investment into the rights and interests. As well, it should adjust the entries so that the long-term stock right investment reports for the parent companies will not be changed.

If some financial statements have been modified just as shown in this step, it will not need to be changed again.

2.4 Computing the Total Number

After compiling the adjusting entries, sum the data from each project of individual accounting reports from parent and subsidiary companies in the consolidated working papers, and compute the summation number of each project separately.

2.5 Compiling the Entries

Compiling the entries and making the offsetting process is the key and main content in the compiling of consolidated financial statement. The main purpose is to counteract the repeated factors of weighted account(or total number) in each project of the individual accounting financial statements, which is, making the offsetting process of the effect that the insider trading has on certain projects in the consolidated financial statements.

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2.6 Computing the Total Number of Each Project in Consolidated Financial Statements

This process is mainly to consider the effect of entries based on the total number of each project in the individual financial statements from parent and subsidiary companies, and then compute the total number of each asset item, debt item, owner's equity item, income item, expense item and so on in the consolidated financial statements separately. The computation method is as follows:

(1) Asset items：The total number is determined by the summation of weighted total amount according to this item and corresponding debit amount minus credit amount in the entries of this item.

(2) Debit items and owner's equity items: The total number is determined by the final result of the weighted total number minus the corresponding debit amount plus the credit amount in the entries of this item.

(3) Income items: The total number is determined by the computation of the weighted total number minus the debit amount plus the credit amount in the entries of this item.

(4) Expense items: The total number is determined by the computation of the weighted total number of this item, plus the debit amount and minus the credit amount in the entries of this item.

2.7 Completing the Consolidated Financial Statements

This process is mainly to completing the official consolidated financial statements according to the computed total number of each project in the asset, debit, owner's equity, income, expense and cash flow chart in the consolidated working papers.

CONCLUSION

In conclusion, the consolidated financial statement is the one that has the most problems and the most complex and controversial problems in the accounting field. Also, it is the most important part in the Chinese CPA test. This paper proposes the suggestions of the normalization of the compiling routine and format improvement of the working papers with regard to the consolidated financial statements, through the analysis of changes in the teaching materials for recent years, and referring some valuable literatures. Those suggestions can help the examinee better understand the compiling process, and improve the comprehensibility and operability of the compiling consolidated financial statements.

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