XVII International Scientific Conference on Industrial Systems (IS'17)
Novi Sad, Serbia, October 4. – 6. 2017.
University of Novi Sad, Faculty of Technical Sciences,
Department for Industrial Engineering and Management
Available online at http://www.iim.ftn.uns.ac.rs/is17

Improving the process of managing by accelerating financial reporting through the implementation of fast closing process

Jelena Demko Rihter
(Assist. prof., Faculty of Technical Sciences, Trg Dositeja Obradovica 6, Novi Sad, jciric@uns.ac.rs)
Emil Živkov
(PhD, Internal auditor, Transnafta, Zmaj Jovina 1, Pančevo, emil.zivkov@transnafta.rs)
Branislav Nerandžić
(Full prof., Faculty of Technical Sciences, Trg Dositeja Obradovica 6, Novi Sad, branen@uns.ac.rs)

Abstract

Internal and external stakeholders need timely, accurate and relevant information for making business decisions. At the same time collecting, processing and disclosure of financial information should be cost-efficient and in accordance to international financial reporting standards (IFRS). System of financial reporting should be designed and implemented in a way that enables compliance of these opposite requests and satisfy information needs of different stakeholders. In a today's business environment companies are faced to extreme high global competition with an additional continuous pressure on reduction of expenses. In order to react adequately and timely to these requests, companies have to improve efficiency of their financial reporting and one of the possible approaches is implementation of monthly fast closing process. The aim of this paper is to introduce the concept of fast closing, advantages that this process enables through the direct approach to the all items of financial reports, as well as its weaknesses and needs for improvement. Authors will focus on the up to date fast closing practice in the companies abroad.

Key words: *efficiency, fast closing, financial reporting*

1. INTRODUCTION - CHANGING ROLE OF FINANCIAL REPORTING

Financial reporting is the process of collecting, consolidating, verifying and disclosure of financial information to external and internal stakeholders. This process takes a time and resources and hence there is constant pressure on its shortenning. Integrated information system contribute to enhancing of this process, but even the large sized companies (with annual revenue over $1 billion) and automated process of financial reporting could not complete each stage of quarterly closing process within one week (Controllers report, 2012).
Disclosure effectiveness is also requested by U.S. SEC (Security and Exchange Commission) and other national regulatory bodies and insitituions on the regulated financial markets. U.S. SEC Division of Corporation Finance set disclosure requirements in Regulation S-K and Regulation S-X in order to provide benefit of both comanies and investors. The aim of these Regulations is to support timely, material disclosure by companies and at the same time to provide information to shareholders. According to Sarbanes-Oxley Act (SOA) and its Section 302 „financial report does not contain any material untrue statements or material omission or be considered misleading“ and „the financial statements and related information fairly present the financial condition and the results in all material respects“. Also according to SOA Sec 409 „Issuers are required to disclose to the public, on an urgent basis, information on material changes in their financial condition or operations.These disclosures are to be presented in terms that are easy to understand supported by trend and qualitative information of graphic presentations as appropriate“.
The role of financial reporting has been exposed to constant changes, moving its focus from the presentation of the historical data to the analysis of financial statements. Financial department should act proacitvely in order to provide relevant and timely information to management and to support the process of making business decisions. At the same time functioning of financial reporting system should be cost efficient. Changing role of financial reporting should be followed by changes of IT system, financial processes and employees which are faced to new challenges. Improvement of system of financial reporting is

necessary in order to provide more qualitative and quantitative information regarding the scarce resources. On the one side are market and regulatory institutions demanding relevant, accurate, transparent and fast information. On the other side are internal and external stakeholders waiting for the relevant, timely, quantitative and qualitative information needed for making decisions, provided at low costs. These mentioned and usually opposite requests should be incorporated in the system of financial reporting. Changes should be reflected in the transformation of financial department shifting its role towards financial analysis (Ernst & Young, 2011).

2. THE TERM AND IMPORTANCE OF FAST CLOSING

Fast closing (FC) is a process of closing the books quickly, usually in a couple of days. It is an important control tool supported by integrated information system that enables fast closing of books of an accounting period, usually a month. According to Janvrin and Mascha (2014) „Financial close process describes a company's ability to complete its accounting cycles and produce financial statements for internal management and external legal reporting working under time (and potential resources) pressure".

The same authors induce and explain the main reasons for increasing attention on fast or financial closing:

- Global economic crisis of 2008 and its consequences reflected in volatile economy that requires timely, relevant and accurate information and performance measures.
- Senior management requirements toward more analysis during the FC process in order to identify internal and external risks and to react timely and properly to potential economic recession.
- New accounting regulation requirements may have negative impact on the efficiency of FC process.
- Audit standards emphasize financial close process as a high-risk area.
- According to some academic researchers the speed of financial closing is an indicator of the quality of a company's internal information environment.

Fast closing is often a key benchmark for effectiveness of finance function and an indicator of corporate health, efficiency and quality of financial processes in an organization. Companies are faced to the increasing complexity of corporate reporting rules, guidelines and regulations, national and international, internal and external, such as IFRS (International Financial Reporting Standards), SOA (Sarbanes-Oxley Act), Basel III, Solvency II, etc. These factors are coming from economic environment and make constant pressure on closing activities tending to slow them. But at the same time new technologies and skilled staff are available to the companies and these factors are under the company control. Company has to disclose accurate, error free and qualitative financial information to the market, as fast as possible and at the same time financial reporting has to be in accordance with the above mentioned corporate regulative and laws.

2.1 Benefits of fast accounting closing

Financial closing of accounting cycles enables fast and accurate information on financial results of an accounting period, contributing to the realisation of the following goals:

- timely financial closing of an accounting period (usually a month) that enables qualitative, quantitative and accurate accounting information
- enabling of permanent monitoring and coordination of fast closing process on the base of document chart flow and defined responsibilities of the participants in the process
- identification of the eventual bottleneck of the process, followed by suggestions of solutions
- setting the rules of monitoring and coordination related to fast closing process

The main purpose of the fast closing process is to present information to the stakeholders in the most propriate way and to facilitate their making decision, having in mind that the shortening of the period of financial closing is not the aim itself. The focus should be set on the preparation for the fast closing process and the time and resources invested in the information technology and training of employees will finally release the time needed for making decisions, business and financial analysis and will enable taking proactive role in the navigation of business towards future.

Bragg (2009) have emphasized a lot of benefits of fast closing process, depends on a point of view of different stakeholders: management, investors, auditors and accountants. Some benefits are:

1. FC provides timely financial information to management, that is of crucial importance by strategic and tactic market positioning.
2. FC is a useful marketing tool that improves investors' trust.
3. FC enables more time to management for financial analysis
4. FC enhances business processes through their detail analysis from the accounting point of view that at the same time minimize accounting mistakes.
5. FC enhances control systems which is of great importance to internal and external auditors.
6. FC enables more time to accountants for doing other activities before and after closing period.

According to the research of the PwC cosultants Eddy, Shipley and Nelson (2004) executives also emhasized the benefits of improving and shortening financial closing and reporting process in their companies:

- 67 % of surveyed executives emphasized that they have more time for analysis and review of reported information;

- 55 % of surveyed executives emphasized increased quality of financial information;
- 48 % of surveyed executives noticed that the decision-making process is more timely and accurate;
- 35 % of surveyed executives noticed that the information from existing system is better;
- 24 % of surveyed executives noticed process alignment and improvement;
- 18 % of surveyed executives highlighted improved credibility in the market and within the organization;
- 14 % of surveyed executives noticed improved staff satisfaction and awareness;
- 6 % of surveyed executives highlighted improved shareholders' confidence.

Although some newest studies have shown that the time that organizations need to make their announcements has no correlation to share price and the benefit of announcing result earlier are limited, there is obvious and concrete benefit reflected in reducing the effort taken to close the books. Also the ability of earlier disclosure leads to potential gains in the financial market and attracting of new investors.

2.2 **Fast closing in the business of multinational companies**

Fast closing of accounting period is especially interesting and usefull for multinational companies which separately apply financial closing at the local and global (consolidated) level. This was also confirmed in the CFO research survey whose results were published in the Controller's report (2012). The main conclusion of this research is that fast closing can be achieved after the reducing the number od the chart of accounts (COA) and centralization of financial consolidation and reporting activities, usually at the corporate or group level. A majority of the respondents (59 %), mainly CFOs (Chief Executive Officer) consider that the consolidate-to report activities should be centralized on the group level. The attitude of the majority of CFOs that took participation in this research could be justified by the fact that the process of accounting closing could be threatened if just one business unit have failed to complete the process on time, regardless of all other business units that have completed processes on time. Another research conducted by Ernst & Young that involved 60 large and medium-sized Danish companies, also showed that the greatest success in reducing financial reporting timeline realized companies that have centralized financial function and integrated IT system. Automation is also needed, but not enough precondition for reducing of closing period and improvement of financial reporting. Automation contribute to performance improvement, but previously it requires standardization and redesign of all processes.

Twenty years ago (1998) when concept of fast closing emerged US-based multinational companies were considerably in advance compared to EU–based multinationals as their global competitors. US-based multinationals managed to automate and standardize their global reporting processes and systems which enabled them to close and consolidate their accounting cycles, do financial analysis and disclose information to stakeholders in a few days. Later close-cycle time in EU-based multinationals were improved but there is still superiority of US-based multinationals regarding elapsed days for public announcement (see the Table 1).

In the Table 1 are shown 34 companies from Global Top 100 that have fastest close cycle regarding public announcement in elapsed days in 2016. There is obvious domination of US multinational companies. Regarding industries the most successful global companies operate in the banking, IT industries (software and hardware), telecommunications, Pharmaceuticals & Biotechnology, retailing, general industrial sector, aerospace and defence. There are only few global are European-based companies ranking on this list.

3. THE IMPLEMENTATION OF FAST CLOSING PROCESS

In order to implement FC management should define by business policy the timeline, materiality levels and size of provisions, as well as to stimulate discipline regarding fast closing task and activities.

According to above mentioned study of the PwC consultants (2004), fast close contains procedures which contribute to:

- Optimization and acceleratation of the closing process;
- Streamline of financial operations;
- Increasing timeliness of information;
- Getting better data quality and more transparent information.

Implementation of FC process is a comprehensive project that defines:

- Responsible business segments, their management and participants in the fast closing of accounting cycles;
- Current and target timelines for recording business transactions;
- Business document flowchart and all needed activities following logic of business processes as a base for recording business transactions in ERP, by each account;

Table 1: Global Top 100 – 30 Fastest by Public Announcement

ED	Y to Y	Company	Subindustry	Country
14	0	JP Morgan Chase	Banks	US
14	-1	Taiwan Semiconductor Manufacturing	Technology, Hardware and Equipment	Taiwan
15	0	Citigroup	Banks	US
15	1	Wells Fargo	Banks	US
17	-2	Oracle	Software and Computer services	US
18	0	Cisco Systems	Technology, Hardware and Equipment	US
19	4	Bank of America	Banks	US
19	-1	IBM	Software and Computer services	US
19	0	Intel	Technology, Hardware and Equipment	US
19	-1	Unilever	Food producers	Netherlands, UK
19	-2	United Health Group	Health Care Equipment and Services	US
19	-1	Wal-Mart Stores	General Retailers	US
21	0	American Express	Financial Services	US
21	-1	Microsoft	Software and Computer services	US
21	6	Schlumberger	Oil & Gas producers	US
21	-1	Union Pacific Corp.	Industrial Transportation	US
21	-1	Verizon Communications	Fixed Line Telecommunications	US
22	-1	General Electric	General Industrials	US
22	2	SAP	Software and Computer services	Germany
23	0	Home Depot	General Retailers	US
23	0	Johnson & Johnson	Pharmaceuticals & Biotechnology	US
25	2	McDonalds	Travel & Leisure	US
26	-1	3M (Minnesota Mining and Mfg)	General Industrials	US
26	-1	AT & T	Mobile Telecommunications	US
27	-7	Banco Santander Central Hispano	Banks	Spain
27	-1	Boeing	Aerospace & Defense	US
27	-1	Facebook	Software and Computer services	US
27	0	Novartis	Pharmaceuticals & Biotechnology	Switzerland
27	1	United Technologies	Aerospace & Defense	US
28	-1	Amazon. com	General Retailers	US
28	1	Amgen	Pharmaceuticals & Biotechnology	US
28	1	Bristol Myers Squibb	Pharmaceuticals & Biotechnology	US
28	0	Roche	Pharmaceuticals & Biotechnology	Switzerland
28	-1	Samsung Electronics Co. Ltd.	Technology, Hardware and Equipment	South Korea

Source: EPMi Close Cycle Rankings 2016, EPM International http://www.epm-international.com/wp-content/uploads/2016/08/EPMi-Close_Cycle_Rankings_2016_Global_Summary_Report.pdf

Legend:

PA – Public Announcement - the date when the year-end financial results are first announced to the stock market

ED - Elapsed days – the number of elapsed days between the company's year end date and the Public Announcement date

Y to Y - Year to Year improvement – the change in elapsed days between this year's PA date and last year's PA date. Positive is an increase, negative is a reduction

Industry/ Subindustry – categorized by Financial Times

- Division of roles, responsibilities and timelines between participant in the process of continuous recording of business transactions in ERP, by each account.

3.1 **Necessity of the process approach in the implementation of fast closing**

Implementation of fast closing (FC) process requires definition of business processes that have impact on financial statements. Working tasks and activities, recognized within business processes, generate recording of business transactions within business segments described in the chartflows. In those chartflows are described activities and timelines in accordance with framework of current and future timelines. Unique mapping of all acitivities that affect changes on accounts is necessary.

Analysis of business process that have impact on financial statements can be presented in the seven basic accounting processes and one controlling process. Cross functional chartflows can be prepared on the base of defined business processes and business transactions, supported by current timelines for each process and document chartflows. Those chartflows should contain schematic description of all main business processes that affect changes in Balance sheeet and Income statement, starting from:

1. Review of production and inventory valuation.
2. Review of billing and indirect taxes.
3. Review of payables and indirect taxes.
4. Review of cash processing.
5. Review of payroll and loans.
6. Review of fixed assets.
7. Review of business transactions recorded in the general ledger.
8. Review of controlling processes related to cost allocation that affect price.

Chartflows contain key current timelines needed for occuring and recording of the business transactions. Current timelines are determined by the character of the business process and dynamics defined by laws, manuals and standards. This approach provides fast and exact information that enables more accurate projection of the final result, as well as possible deviation from the planned or target values.

Process approach requires implementation of comprehensive IT ERP solution. Business transaction is recorded immediately after the end of an activity, e.g. receiving and shipping of goods. Hence accounting requires process approach, too.

In the study of Ernst & Young (2011) have been identified 10 recommendations for improving the process of financial reporting:

1. Setting the process of continuous improvement of financial reporting as a permanent task.
2. Special attention should be devoted to the business processes and IT systems, i.e. optimization of business process and IT systems has a key role in the process of change management.
3. Cross-functional division of roles and responsibilities for all related activities and participants in the financial reporting should be done.
4. Complete finance manual should be done and available for all participants in the process of financial reporting. Manual should be an overview of accounting policies, chart of accounts, deadlines, roles and responsibilities, as well as handling of master data.
5. Define the process for efficient resource and skill management, i.e. monitor the process in order to find bottlenecks and unutilised capacities; special attention should be devoted to the development od skills.
6. Standardization of processes, procedures, internal controls and enabling more uniform reporting.
7. Define complete timelines of reporting acitivities, with precious start and end times for each activity and use it permanently as a management tool.
8. Automatization of processes and procedures in the IT system. Automatization of processes and controls enhances the speed of the process and reduces the financial reporting errors.
9. Reduce the risks associated to IT spreadsheets – it is reccommended to use ERP systems or transparent and consistent spreadsheets.
10. Acceleration of activities.

Numerous mentioned and recognized activities which slow down or accelerate financial reporting require focus on this problem. Implementation of fast closing demands process approach, which means that a team should analyse all business processes in detail. Suggestions for process improving should be done after the analyse of processes and recommended changes should be realized. Realization of activities requested for the fast closing implementation considerably reduce the time for closing of accounting cycles and preparation of periodic financial reports (e.g. in the most succesful companies this process requires only 3 days). Described effects are shown on the Figure 1.

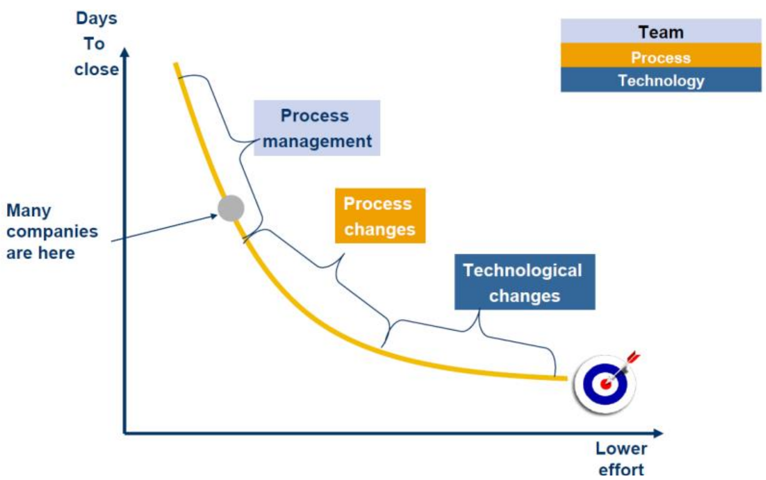

Figure 1: Effects of implementation of fast closing process

Figure shows that focus in the fast closing implementation is on the change and modelling of current and thier derivative accounting processes. Nonetheless implementation and following redesign of comprehensive IT systems requires process approach too, in order to decompose processes to subprocesses. Comprehensive IT systems, such as ERP and Business intelligence record business transaction at the point of occurance, i.e. instantly at the end of each activity such as: receiving and shipping of materials and goods, billing, payables, cash inflows and outflows, etc. Hence accounting requires process approach to all items of financial statements.

4. CONCLUSION

Fast closing is a standardized process of completing accounting cycles of the period and preparing internal and external reports. It requires special, process approach to accounting, but other functions in the company too. Implementation of the fast closing requests engagement of all business functions, followed by redesign of business processes regarding to forms and timelines of financial reporting. These changes are useful for the accounting, but other business functions too and contribute to improvement of the complete process of management. Processes such as flow of accounting documents, valuation of production and inventories and other should be redesigned which requires higher level of their automatization. Nowadays some ERP systems have own moduls for fast closing that enables following of the complete flow of activities related to closing of accounting cycles.

Faster financial reporting enables earlier disclosure of quantitative and qualitative information to the market which can lead to the better and timely decision-making of external stakeholders. At the same time successfully implemented fast closing process save a company huge resources (time and money) reducing staff needed for financial reporting, having in mind that after accelerating of closing activities management will have more time and attention could be put on analysis and making descisions. This will result in improving of managing process in the company.

5. REFERENCES

[1] Bragg, S. (2009), *Fast close – A guide to closing the books quickly*, John Wiley and Sons, USA.

[2] CONTROLLERS REPORT, (2012), Centralization - not Automation - Is Key to Achieving the 'Fast Close', pp. 2-3.

[3] Eddy, S., Shipley, W,R., Nelson, D. (2004), SAP Functionality to Support Fast Close, PwC and SAP Sarbanes Oxley; Web Conference Series

[4] Ernst & Young, (2011), Closing Excellence –An analysis of the financial reporting process of 60 large and medium-sized Danish companies http://www.ey.com/Publication/vwLUAssets/Closing_Excellence,_november_2011,_UK/$FILE/FAAS%20analyse%20-%20Closing%20Excellence%20-%20UK.pdf

[5] Janvrin,D., Mascha, M. (2014). The Financial Close Process: Implications for Future Research, *International Journal of Accounting Information Systems,* 15, pp. 381-399.

[6] PWC, (2013), Close Cycle Report, Rankings for the 2013 R2R External Reporting Process http://www.pwc.co.uk/finance/finance-matters/insights/close-cycle-report-2013.html

[7] http://pwc.blogs.com/finance_matters/2016/10/closing-the-books-on-fastclose.html

[8] Živkov, E., (2015), Development of the model of internal control mehanisms in the function of managing of the company, PhD thesis, Faculty of technical sciences Novi Sad, University of Novi Sad.