ASPECTS OF FINANCIAL CONSOLIDATION AT GROUP LEVEL

BY BEAT HAERING AND NICOLE FLÖTHE
FROM CAREY GROUP, ZURICH.

beat.haering@careygroup.ch
nicole.floethe@careygroup.ch

In most countries groups of companies of a certain size are required to prepare consolidated financial statements. Normally this is seen as an unpleasant obligation, while the business advantages of consolidations are often ignored.

Even for groups that do not exceed the size criteria, there are frequent situations where consolidated figures are required, such as finding new equity investors, negotiations with banks for new credit lines or in the execution of succession plans.

BENEFITS OF VOLUNTARY CONSOLIDATION

Usually the need to provide consolidated group figures by third parties is experienced as an unpleasant obligation. It is often ignored that consolidated group figures offer numerous advantages which can lead to better decision making in many situations. Therefore, the consolidation of group figures on a voluntary basis should be considered. The following four examples will illustrate this proposal:

1 COMPANY ACQUISITIONS/ DISPOSALS OR DEBT FINANCING

In the case of a projected acquisition or disposal of a company or debt financing it is advisable to perform analysis of the effects of the transactions on the financial position of the group as a whole before it is executed. To do this consolidation simulations are available which visualise, not only the changes in assets and liabilities on both sides of the balance sheet, but also identify changes in earnings, cash flow statements and KPI's

2 PERFORMANCE MANAGEMENT

The quality of consolidated figures is reflected in depth and, in particular, the analysis of information provided. The decision-supporting numerical data can create many benefits for the company: cost reduction potential, early detection of deviations from planning or the development of individual revenue sources are examples of the leads that an appropriate management information system can provide for decision makers. In addition causes of problems can be easily identified and therefore fixed. Used consistently, the results of the performance management should far exceed the costs of the consolidation.

3 CURRENCY SHIFTS/CHANGES IN EXCHANGE RATES

For international groups which have cross-border supply chains in countries with different currencies, changes in exchange rates represent permanent challenges.

An overview of the financial status and the development of such a group can by default only be achieved at a consolidated level using a consistent reporting currency. Highly functional consolidation systems also allow for simulation analysis and can make the necessary calculations of foreign exchange reserves shown in the group´s equity much easier and the presentation more comprehensive.

4 GENERATION CHANGE/ SUCCESSION PLANNING

In most cases where the management of a company is handed over to the next generation or, as part of the succession process to external management, the previous management generation still advises the company in order to ensure a smooth transition. In these cases, a consolidated financial status helps to get a fast and accurate overview of the development of the group of companies whilst also helping to prevent the misunderstandings that frequently occur with successions.

SPREADSHEET OR CONSOLIDATION SOFTWARE?

Regardless of whether the requirement to prepare consolidated figures is based on legal provisions, requirements from the capital markets or management requests for better decision making, the affected departments are faced with new challenges for which they are usually ill-prepared. It is understandable that initial consolidations, often on an ad-hoc-basis, are carried out on spreadsheets but it is incomprehensible that around two thirds of all consolidation work performed around the world continues to be done this way.

Particularly in groups that operate internationally and have subsidiaries subject to consolidation or investments in countries with different accounting principles and exchange rates, spreadsheet solutions are fast becoming confusing. It must also be ensured that relevant changes in accounting regulations are reflected over time. After a few years, extensively linked spreadsheets, containing many formulae develop with such complexity that errors can become difficult to detect.

The time factor must also be considered: using spreadsheet solutions the collection and consolidation of data accounts for the majority of the time invested. As a result, too little time remains for the much more important tasks of analysis and discussion of the results. Software solutions significantly reduce the burden of data collection through automation of the consolidation process. Therefore, more time is left for the interpretation of the results and the formulation of operational and/or strategic measures.

Additionally, there is the risk of errors which can be critical for a company, for example consolidated figures are often required in application for loans and errors can lead to rejection or significantly worsened terms. Furthermore, the use of spreadsheets in such scenarios increases the dependency on individuals who are responsible for the consolidation significantly.

CONSOLIDATION SOFTWARE: BUY OR OUTSOURCING?

When a company opts to use consolidation software, it decides whether the software should be acquired or whether the consolidation project is to be handled through a service provider. Highly specialised providers, with extensive experience in the preparation of consolidated figures and equipped with powerful software tools, are not only able to significantly reduce the costs that arise with the project's implementation, but can also provide added value at the same time.

In addition, the cost aspect must withstand an objective analysis: whereas the outsourcing solution, with the exception of special services, typically consists only of clearly calculable monthly charges the outright acquisition of software involves a variety of hidden costs which are often overlooked in the decision-making process. To name a few, the cost of implementation often requires the hiring of external consultants in addition to the requirement for internal resources, annual maintenance and support costs, training of staff, additional costs for further licenses as and when these are required by the company's growth, and software extensions (in particular reporting and analysis tools). If consistently applied, performance management results could far exceed the additional costs of consolidation.

CONCLUSION

Good corporate governance is forward-looking and active, and this implies the existence of timely, customised management information. Efficient controlling is essential especially in the digitised world with its rapid and unpredictable changes. Opportunities and cost/benefit-aspects of outsourcing solutions should always be included in such considerations. The availability of consolidated figures prepared by a sophisticated system can quickly become a catalyst for the future success and viability of the company.

REQUIREMENTS TO CONSOLIDATE IN THE UK

The preparation of consolidated financial statements for groups of companies in the UK are prescribed by FRS 102 and section 383 of the Companies Act 2006. It provides a waiver for companies that in two subsequent financial years do not exceed two of the following three size criteria: aggregate turnover: £10.2 million net (or £12.2 million gross), aggregate balance sheet total: £5.1 million net (or £6.1 million gross), aggregate number of employees: 50.

Similar rules apply to other European countries.

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