

Some thoughts on recovering and improving statement of enterprise profit distribution

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ABSTRACT: This thesis demonstrates the reasons for recovering and improving statement of enterprise profit distribution by analyzing the problems existing in enterprise profit distribution and disclosure. It has made it clear that there shall be distinction between profit formation and profit distribution. Recovering statement of enterprise profit distribution can better disclose the situation of profit distribution and show each stakeholder's participation with enterprise profit distribution in "white-box" status, in order to make it convenient for research on whether the contribution made by each production factor can match corresponding distribution.

Keywords: statement of profit distribution; recovery; improvement

1 INTRODUCTION

With the development of the times and the progress of Enterprise profit distribution has obtained great attention from all circles in China all the time. Lei Yin^[1] (2006) analyzed all the factors which could affect the level of enterprise profit distribution, and proposed to improve mandatory dividend system so as to enhance the disclosure of enterprise profit. However, disclosure of reasons for pre-arranged cash bonus planning was not included in his proposal. Xue'an Zhang^[2] (2007) thought employees who had made part human capital specific investment should also obtain part surplus of enterprise profit. Chi Cui, Xizai Jin, and Shijun Qu^[3] (2009) thought enterprise system with acknowledgement of direct right to use labor force shall be established so as to grant labor force the right to participate in profit sharing. Wenxiu Xu^[4] (2010) concluded the research progress of state-owned enterprise profit distribution, and emphasized on the participation of human capital in state-owned profit distribution. Haizhou Pi^[5] (2010) thought there were many problems prevailing in the profit distribution of listed companies in our country, such as "non- distribution", "no participation in profit", high stock dividend and high cash dividend, and refinancing of giant sum. Aimei Cai^[6] (2011) also did research on related

problems in the profit distribution of listed companies in our country. Ke Wang^[7] (2012) thought the enterprise profit distribution system in our country was in need of further improvement and was lack of stability and sustainability. He thought it was inevitable to improve bonus system. Zhang Luo and Xiao Liu^[8] (2012) thought the relation between state-owned enterprises and the government had evolved from antagonistic to mutual beneficial in profit distribution pattern. Xiaohui Li and Chao Li^[9] (2013) thought proofs for enterprise profit distribution were not clear and had led to the lack of impetus in the enterprise profit sharing at that time. Erzi Tang, Fengchao Liu and Na Zhang^[10] (2013) found the influence that production technology had on enterprise profit distribution and national economic development through decision-making study of microcosmic corporate behaviors. Nan Zhang^[11] (2015) pointed out the profit distribution of listed companies in our country had problems of weak awareness of profit sharing, unequal profit sharing, and moral hazard. The research outputs about profit distribution problems mentioned above are fruitful; however, few of them involve research on profit distribution disclosure. Under the background that there's no sufficient theoretical proof for the cancellation of statement of enterprise profit distribution and consolidated statement of profit distribution regulated by the ASBE (Accounting Standards for Business Enterprises) carried out in 2006 and related in-

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fluence is in underestimation, this thesis plans to propose the recovery and improvement of statement of enterprise profit distribution based on analysis of enterprise profit distribution and disclosure of the existing problems, and to clarify the reasons so as to make the enterprise profit distribution in our country clearer and more “white-boxed”.

2 ANALYSIS OF PROBLEMS EXISTING IN ENTERPRISE PROFIT DISTRIBUTION AND ITS DISCLOSURE

2.1 *Problems existing in the enterprise profit distribution*

2.1.1 *Unequal profit distribution*

As the principle set for the primary distribution in our country was “efficiency-oriented with balance in equity”, unequal distribution between human capital and non-manpower capital has existed for a long time with no proper resolution. Moreover, the failure to rectify the principle in secondary distribution has aggravated the unequal distribution to some extent and led to serious polarization of wealth distribution. According to the data published by NBS (National Bureau of Statistics) in 2014, the Gini coefficient of China has reached 0.469.

2.1.2 *Insufficient participation of human capital element in distribution*

Report of the 18th NPC (National People’s Congress) emphasizes on the “primary distribution mechanism in which the participation distribution of related elements including labor, capital, technology and management shall be arranged according to their contributions”. However, the implementation of the regulations set in the documents published by our party and government into “institutional” arrangement is not enough. Specific carried out distribution system is lack of sound arrangement in legal system^[12]. As direct participation in surplus value distribution can bring much more incentive to employees than employee compensation; non-manpower capital contains much more impulse for surplus value than human capital; and effective motivation brought by human capital is not enough under knowledge information social conditions, it is very hard to reach an all-win situation for all stakeholders. The reality of current enterprise profit distribution is as follows: collective consultation mechanism on wages is unsound; principal part of surplus value is still “distributed according to capital”; non-manpower capital participates in surplus value distribution (shareholders can get dividend while creditors can get interest); and human capital cannot participate or can only participate in little part of surplus value distribution, meaning part technical personnel can participate in certain surplus value distribution as in-

tangible asset admission, and a few enterprise senior executives can participate in surplus value distribution in forms of annual salary and stock option while the vast general staffs cannot participate or can only participate in little part of surplus value distribution.

2.1.3 *Proofs for enterprise profit distribution are not clear*

The standards for each enterprise or even the parent-subsidary corporations belonging to the same enterprise can be different. The differences mainly manifest on the proof of enterprise profit distribution to judge whether the distribution shall be completed based on the profit available for distribution of the company or that in the consolidated statement. No clear proof can be found at present.

2.1.4 *“Cash dividend rate” of enterprise is low*

According to the studies recorded in Reference^[5] and Reference^[6], the following situation is common in the listed companies: no distribution, leaving investors’ both hands empty; no dividend, replacing investment return by stock dividend; high participation in profit, turning capital of listed company into substantial shareholder’s bonus; and cash dividend on one hand with giant sum refinancing on the other hand.

2.2 *Problems existing in disclosure of enterprise profit distribution*

2.2.1 *The disclosure boundary between profit formation and profit distribution is unclear*

According to the definition set in our ASBE (Accounting Standards for Business Enterprises), the substance of profit is net profit after deducting interest and income tax. According to stakeholder theory, interest shall belong to creditor’s participation of interests while income tax shall belong to governmental participation of interests of which the substance is within profit distribution. Thus, “earning distribution view” shall be taken instead of “expense view”. As a result, profit formation and profit distribution cannot be mixed together. Items belonging to profit distribution have been disclosed in profit statement. There’s no clear boundary between profit formation and profit distribution. Hence, adjustment shall be done in related disclosure.

2.2.2 *Presentation of profit formation has been emphasized on while presentation of profit distribution has been paid little attention to*

In our ASBE, profit statement has been maintained while statement of enterprise profit distribution and consolidated statement of profit distribution have been cancelled. ASBE thinks statement of changes in owner’s equity can replace statement of profit distribution. In fact, it is a reflection that presentation of profit formation has been emphasized on while presentation

of profit distribution has been paid little attention to. Statement of changes in owner's equity can only disclose information about owner's profit sharing. However, profit distribution is an important part in enterprise management activities. It is profit distribution of all stakeholders instead of owner's profit distribution. Information about all stakeholders' participation in profit sharing shall be disclosed in details.

2.2.3 *Disclosure is untrue in content and lack of standardization in format*

Some enterprise management executives deliberately make the operation state better than the actual situation for their own good. In profit distribution, they purposely use unstandardized accountant arrangement methods to mislead information users. As a result, other stakeholders will suffer from loss in their legitimate rights and interests.

2.2.4 *Disclosure is insufficient and not in time*

Many enterprises, especially listed enterprises, fail to disclose their enterprise profit information and profit distribution in details in a timely and accurate way. For example, there's no detailed explanation for where exactly enterprise profit comes from or where profit is distributed.

3 REASONS FOR RECOVERING STATEMENT OF ENTERPRISE PROFIT DISTRIBUTION

3.1 *Proofs for cancelling statement of profit distribution are insufficient*

It can be seen from analysis of research literature and learning materials related to ASBE that we have not conducted sufficient theoretical analysis or feasibility research on cancelling statement of profit distribution. Statement of profit distribution and consolidated statement of profit distribution have been cancelled to follow IAS (International Accounting Standards) based on ideas shown in No.1 Code of IAS- Presentation of Financial Statements. Meanwhile, we have not made sufficient estimation on the adverse impact that cancellation of statement of profit distribution will bring and have paid too little attention to the importance of it. Neither has comprehensive disclosure been made to the participation of labor element, capital element, technology element or management element; nor have we taken sufficient consideration of the requirement in our socialism with Chinese characteristics-people shall be the master of their country and obtain common prosperity. Cancelling statement of profit distribution is against the principle of openness, fairness and impartiality. "System" arrangement and disclosure mechanism with participation of human capital in surplus value distribution shall be established. Therefore, it is not cautious enough to cancel statement of profit distribution.

3.2 *Statement of profit distribution cannot be replaced by statement of change in owner's (shareholder) equity*

Statement of changes in owners' (shareholders') equity is mainly used to reflect the increase and decrease of each constituent part of owner's equity in current period. The profit distribution information provided by statement of changes in owners' equity is not complete for most of it is disclosed according to owners' needs instead of all stakeholders' side. Thus, it cannot replace statement of profit distribution. Although statement of changes in owners' equity can list part items related to profit distribution, the listed information is nowhere close to the comprehensiveness of the information contained in statement of profit distribution. Statement of changes in owners' equity emphasizes on disclosure of owners' sharing information, but pays little attention to disclosure of other stakeholders' sharing information. Moreover, it cannot disclose each kind of owner's profit distribution in details, such as preferred stock dividend payable and common stock dividend payable.

3.3 *Profit formation and profit distribution should be individually disclosed*

Profit statement only reflects profit formation while statement of profit distribution only reflects profit distribution. Presentation of profit distribution and that of profit formation shall be equally treated and shall not be crossed or repeated. Both shall be separately disclosed. As the profit defined in ASBE actually refers to net profit after deducting financial expenses (interest) and income tax, interest and income tax shall belong to the range of profit distribution and listed in statement of profit distribution. Our ASBE shall coordinate with IAS instead of aimlessly following it. Blindly following foreign profit statement to reflect EBIT and net profit while cancelling statement of profit distribution is definitely not a smart choice for us as the reason for why western countries exclude human capital from profit sharing might be covering up their exploitation. Therefore, the writer of this thesis suggests amending the definition of profit set in ASBE. It shall be profit (without deduction of interest or income tax) instead of net profit. In the meantime, we shall also recover and improve statement of profit distribution and place all stakeholders' participation in enterprise profit distribution in "white-box" status. Dividend, interest, tax, human capital (labor, technology, and management) and participation in after-tax sharing shall all be included and disclosed in statement of profit distribution.

4 IMPROVEMENT ON STATEMENT OF ENTERPRISE PROFIT DISTRIBUTION AND REASONS FOR IMPROVEMENT

4.1 *Format of improved statement of enterprise profit distribution*

Based on the above analysis, we have made the format for improved statement of profit distribution as shown in Table 1 which can be directly used as the master table of accounting statement or as the annexed table of profit statement.

4.2 *Reasons for improvement on statement of enterprise profit distribution*

4.2.1 *It can make a clear distinction between profit formation and profit distribution disclosure*

Western countries include interest and income tax in the subtraction items of profit and loss after calculating EBIT (Earnings before Interest and Tax) in income and loss statement. As a result, what they reflect is net profit or loss, and thus the disclosure boundary between profit formation and profit distribution is not clear enough. Although our profit statement shares different connotation and display order of related items with that of western countries, the “interest ex-

penses” and “income tax expense” in our profit statement have been disclosed as “financial expense” and “income tax expense” respectively for a long time. As the economic explanation of interest and income tax should be included in the distribution of surplus value, we don’t think they should be disclosed in profit statement; instead, they should be disclosed in profit distribution as “interest sharing” and “income tax sharing”. Correspondingly, the accounting title of “financial expense” shall be canceled. Related managerial expenses such as transfer commission shall be included in “management expense”. “Interest sharing” shall be individually set up for the business accounting of non-capitalized interest expense. Moreover, “income tax expense” shall be changed as “income tax sharing”.

4.2.2 *It is implementation of the income-distribution policy regulated by CPC (Communist Party of China) and the government*

In recent years, our overall resident income has been increased; however, its proportion in national income distribution has been decreased. Our party and govern

Table 1. Statement of profit distribution

Statement of XX

Name of enterprise: ××

20××

Unit: Yuan

Item	Line No.	Actual Amount in Current Year	Actual Amount in the Past Year (Skipped)
1.Earnings before interest and taxes (also known as EBIT)	1		
Subtract: interest sharing	2		
Income tax sharing	3		
2.Net profit	6		
Add: early undistributed profit	7		
Other transfer-in	8		
3.Profit available for distribution	11		
Subtract: Withdraw legal accumulation fund	12		
Withdraw discretionary surplus reserve	13		
Labor element sharing	14		
Technological element sharing	15		
Management element sharing	16		
Or withdraw bonus and allowance bond	17		
Withdraw reserve fund	18		
Withdraw reserve for business expansion	19		
Investment returned with profit	20		
4.Profit available for owners distribution	23		
Subtract: Preferred stock dividends payable	24		
Common stock dividends payable	25		
Common stock dividends shifted as capital (or capital stock)	26		
5.Undistributed profit	29		
6.Earnings per share	30		
(1) basic earnings per share (basic EPS)	31		
(2) diluted earnings per share (diluted EPS)	32		

-ment pay high attention to income distribution. Report of the 18th NPC emphasizes that “both primary distribution and redistribution shall give consideration to efficiency and equity while redistribution shall pay more attention to equity”, and “principle in which the sharing distribution of related elements including labor, capital, technology and management being arranged according to their contributions shall be established while distribution system in which distribution according to work is the main body with multiple distribution forms coexisting shall be improved”. The bulletin of the 18th Plenary Session has also emphasized to “form reasonable and orderly income-distribution structure” so as to reach consensus that production elements, including human capital (labor, technology and management) and non-manpower capital, can participate in distribution according to their contributions (not limited to sharing in distribution of labor reward, but can also participate in surplus value sharing, especially in distribution of after-tax profits), meaning that only when human capital and non-manpower capital can share enterprise residual claim, “can all the fountains that create social wealth be sufficient and maintained”. Therefore, human capital and non-manpower capital should be the principal part to share equal profit (especially after-tax profit) distribution. Sound mechanism and procedure (including arrangement in legal system) for the participation of human capital (labor, technology and management) in after-tax profit distribution shall be established; and it shall be applied in enterprise practice and take the test from practice while emancipating our minds. Recovering statement of enterprise profit distribution can better disclose the situation of profit distribution. Improving statement of enterprise profit is to better improve the disclosure of the participation of human capital in enterprise profit distribution. The situation of all stakeholders’ participation in enterprise profit distribution shall be placed in “white-box” status so as to make it convenient for analysis and research on the contribution of each element and for the judgement on whether the contribution of each element can match their distribution. Recovering and improving statement of enterprise profit distribution is not only required in implementing the income-distribution policy regulated by our party and government, but is also required in disclosing the situation of each production element and enterprise profit distribution. In the meantime, it can better accord with the understandability principle and help realize openness, equity and impartiality.

4.2.3 *It can bring further optimization to profit distribution procedure*

Net profit (also known as net profit or loss) can be obtained by subtracting interest sharing and income tax sharing from the gross profit of enterprise in current period. Profit available for distribution can be obtained by combining net profit with early undistrib-

uted profit (or subtracting early undistributed deficit) and other transfer-in balance. Profit available for distribution in current year can be distributed in the order as follows:

- (1) Confiscated property loss; overdue fine and penalty for payment of each tax;
- (2) Compensation for the AT (after-tax) loss of previous year;
- (3) Withdrawal of legal accumulation fund by 10% of after-tax profit;
- (4) Withdrawal of free surplus accumulation fund according to resolution of shareholders’ meeting;
- (5) For ordinary enterprises, present calculated labor element sharing, technology element sharing, and management element sharing according to distribution principle of production element sharing based on contribution;
- (6) For foreign-invested enterprises, present withdrawal of employee incentive and reserve funds, welfare fund, enterprise development fund, and investment returned with profit;
- (7) Distribute the dividend or profit for all owners. Companies limited by shares shall distribute dividend according to shareholder’s shareholding ratio, including dividend of preferred share (stock dividend) and dividend of ordinary share (bonus). Limited liability companies and other enterprises shall distribute profit to shareholders or owners according to their ratio of investments.

Undistributed profit (or undistributed deficit) of enterprise can thus be formed through the distribution order mentioned above. Undistributed profit can be remained for distribution afterwards.

4.2.4 *It can bring corresponding adjustment to other statements*

In addition, cash flow statement shall add “cash related to payment for labor, technology, and management elements” in “cash flow generated in business activities”, or merge “cash related to payment for labor, technology, and management elements” with cash paid to/for employee. Correspondingly, “labor, technology, and management element sharing” shall be added in “profit distribution” of statement of changes in owner’s (shareholder) equity. Earnings per share shall also be disclosed in statement of profit distribution instead of profit statement. In the meantime, corresponding adjustment shall also be completed in corresponding items of consolidated statement of profit distribution.

5 CONCLUSIONS

Profit distribution disclosure is to disclose the process and results of the profit distribution participated by each stakeholder in details. Profit distribution justice is to grant equal qualification and even opportunities to both human capital and non-manpower capital in

profit distribution. It aims to reach better matching between the contribution of each production factor and the corresponding results. As a requirement set in socialist market economy, profit distribution justice is also a target pursued by the vast stakeholders. Recovering and improving statement of enterprise profit distribution can fairly, impartially and clearly present detailed process and results of profit distribution to the public, containing great theoretical significance and practical value.

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