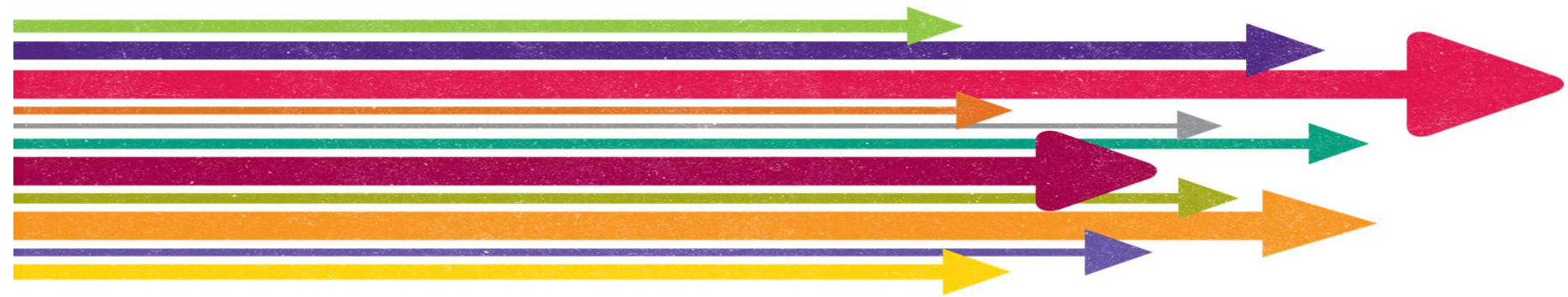


Walker Chandiook & Co LLP

## Common Errors in the Presentation of the Financial Statements under the Companies Act



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For ICAI – WIRC, Baroda Branch, 14 May 2016

# Contents

Errors in presentation of the Financial Statements with respect to provisions of

**Accounting Standards**

**Schedule III**



# Instances of non-compliance with Accounting Standards



## AS 1 – Disclosure of Accounting Policies

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- Accounting policies were given under various notes to accounts as against stating all the policies under a single head titled, 'Significant Accounting Policies'.
- Significant Accounting Policies uses ambiguous terms, viz. 'in applicable circumstances'. Situation under which such policy has been adopted is not explicitly disclosed
- In accounting policy for revenue recognition, the point of time for revenue recognition is not stated explicitly
- Unrealised losses disclosed in the Balance Sheet through notes, but not been recognised in the financial statements.

# AS 1 – Disclosure of Accounting Policies

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- Omission to disclose the significant accounting policies with regard to one or more of the following:
  - Valuation of Inventories
  - Net profit or loss for the period, prior period items and changes in accounting Policies
  - Revenue recognition including interest income
  - Accounting for Fixed Assets
  - Foreign Currency Transactions
  - Accounting for Investments
  - Use of estimates
  - Impairment of assets

## AS 2 – Valuation of Inventories

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- In accounting policy for valuation of inventories, policies adopted in measuring inventories is not disclosed.
- Guidance note on Audit of Inventories, issued by the ICAI clarifies that use of the expression 'as valued and certified by the management', may lead the users of financial statement to believe that the auditor merely relies on the management's certificate and that there is a disclaimer; such reference should be avoided

## AS 2 – Valuation of Inventories

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- Provision of Excise Duty on the closing stock of Finished Goods is not created and hence not considered for the purpose of valuation of inventory lying in the factory or bonded warehouse
- 'Average cost' method used for the determination of cost of inventory
- All the cost incurred in bringing the inventory to its present location and condition not considered to determine its value (Costs like indirect overheads, depreciation, etc. not considered)

## AS 3 – Cash Flow Statements

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- Movement in borrowings and purchases or sales of investments/ fixed assets reported on net basis
- The effect of changes in exchange rates on cash and cash equivalents held in a foreign currency is not reported as a separate part of the reconciliation of the changes in cash and cash equivalents during the period
- Cash and cash equivalent balances not available for use is not disclosed separately.
- Payment or refund of income taxes is not specifically identified and separately disclosed for financing and investing activities



## AS 3 – Cash Flow Statements

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- All non cash items in financial statement are not adjusted in cash flow statement.
- Change in each component of current assets and current liabilities not disclosed separately for adjustment in working capital
- Disclosure of changes in restricted bank balances (other than Cash & Cash Equivalent) under operating activities

## AS 5 – Net Profit or loss for the period, Prior period items and changes in Accounting Policies

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- Nature and amount of prior period items is not disclosed separately
- Nature and amount of extraordinary item is not separately disclosed
- Amount of exceptional item is not separately disclosed

## AS 5 – Net Profit or loss for the period, Prior period items and changes in Accounting Policies

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- Nature and amount of a change in an accounting estimate which has a material effect in the current period or which is expected to have a material effect in subsequent periods is not disclosed
- Impact of change in accounting policies is not disclosed on current year profit, i.e. additional depreciation charged during the year

## AS 9 – Revenue Recognition

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- Sales (net of excise duty) shown on the face of the Statement of Profit and Loss as well as in the notes. The amount of excise duty deducted from sales has been indicated in the schedule to the Profit and Loss Account by way of narration only
- Difference in excise duty on opening and closing stocks of finished goods disclosed in the schedule of material consumed
- Sales includes the consignment sales

## AS 9 – Revenue Recognition

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- Dividend income recognised on receipt basis
- Self consumption of goods produced are included in the figures of sales
- Inter divisional transfers of goods, as marketable products produced by separate divisions of the company for captive consumption are made as if sales were to third parties at current market prices and are included in turnover

## AS 11 - The Effects of Changes in Foreign Exchange Rates

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- Transactions relating to purchases and sales of goods and services denominated in foreign exchange were translated to Indian Rupee by applying the rate prevailing on settlement
- Gain or loss arising due to exchange fluctuations were adjusted against revenue
- Notes to accounts indicated significant foreign currency transactions; Exchange gain or loss was neither disclosed in the Profit or Loss Account nor in the notes to the accounts

## AS 11 - The Effects of Changes in Foreign Exchange Rates

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- If net impact of foreign exchange fluctuation is nil then the effect should be disclosed separately by way of notes to the accounts
- Non-monetary assets/ liabilities of the company were converted at the closing exchange rate. Further, some monetary items not converted at the closing exchange rate

## AS 13 - Accounting for Investments

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- Profit from sale of investment not bifurcated into income from long-term investment and current investments and/ or trade and other investments
- Investment not classified into Long-term investment and Short-term investment. Long term investment not been classified into Trade investment and Other investment.
- A company invested in various units and bonds but accounting policy as adopted for its valuation had not been disclosed



## AS 13 - Accounting for Investments

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- Non-disclosure of aggregate market value of quoted investments/ unquoted investments and the nature of such investments
- Policies on valuation of long-term investments not in line with the requirements of AS 13

## AS 15 – Employee Benefits

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- Omission of disclosure of the amounts for the current annual period and previous four annual periods of:
  - the present value of the defined benefit obligation, the fair value of the plan assets and the surplus or deficit in the plan;
  - the experience adjustment arising on the plan liabilities and assets expressed either as an amount or percentage of the plan liabilities and assets respectively at the balance sheet date

## AS 15 – Employee Benefits

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- Omission of disclosure of the employer's best estimate of the contribution expected to be paid to the plan during the annual period beginning after the balance sheet date
- Accounting policy for recognition of employee benefits under defined contribution scheme states that expenses are recorded as they fall due

## AS 16 - Borrowing Costs

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- Amount of borrowing costs capitalised during the period not disclosed
- Restructuring charges which had been paid to extinguish high cost debts were written-off over the tenure of fresh loans taken for refinancing such high cost debts
- Premium on prepayment/ resetting of interest liability on term loans amortised over the remaining repayment period of loans

## AS 18 - Related Party Disclosures

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- Disclosure of significant related party transactions not in line with AS 18
- Separate disclosure of **material** related party transaction not made, instead merged with other similar nature transactions
- Different nomenclature used under the Related party disclosure *vis a vis* the financial statements
- Either name of the related party or the nature of relationship or both not disclosed where control exists with related party

## AS 22 – Accounting for Taxes on Income

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- Non-disclosure of deferred tax assets recognised to the extent of deferred tax liability as on the balance sheet date, in the absence of virtual certainty for recognition of deferred tax assets
- An enterprise has unabsorbed depreciation or carry forward of losses under tax laws and nature of the evidence supporting the recognition of deferred tax assets not disclosed in financial statement

## AS 22 – Accounting for Taxes on Income

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- Provision for current tax and deferred tax have been clubbed and disclosed under the single head of 'provision for taxation'
- Break-up of deferred tax assets and liabilities in the balance sheet not disclosed into major components of the respective balances
- Projection of future profits made by an enterprise considered as convincing evidence for recognition of deferred tax assets

## AS 26 - Intangible Assets

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- Amalgamation expenses/ preliminary expenses/share issue expenses/miscellaneous expenses have been capitalised under the head of 'Deferred revenue expenditure'/ 'Miscellaneous expenditure' and amortised over a period of 3-5 years
- Certain companies recognised intangible assets in their Balance Sheet viz. computer software, technical know-how, development expenditure etc. but no other information (viz. useful life, amortisation method adopted etc.) relating to such assets has been provided in the financial statements. Incomplete disclosures made in financial statement



## AS 26 - Intangible Assets

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- Expenditure on research and development recognised as expense is not separately disclosed
- Amortisation period for intangibles viz. Brands and Goodwill is stated to be 20 years; basis for taking a longer period of amortisation not specified

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# Instances of non-compliance with Schedule III



## Instances of non-compliance with Schedule III (1/3)

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- Omission of disclosures required for Share Capital
- Showing debit balance of profit and loss in excess of uncommitted reserves on the assets side of the balance sheet
- Non-disclosure or partial disclosure of repayment terms of vehicle loans, issue of bond or debentures etc.
- Reporting substantial amount of long term liabilities under the head 'others' without specifying the nature of such liabilities

## Instances of non-compliance with Schedule III (1/3)

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- Presentation of 'Sundry creditors' as separate line item under the head 'current liabilities', instead of as 'Trade payables'
- Using the term 'Sundry Creditors', as it may include dues other than that in the nature of trade payables, such as, statutory dues payables, other contractual obligations that may not have occurred due to goods purchased or services received
- Presentation of liabilities towards employee benefits as 'Short term provisions' only

## Instances of non-compliance with Schedule III (1/3)

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- Grouping of expenses incurred on the intangible assets still under development under the head 'Capital work-in-progress'
- Presentation of addition and deletion to fixed assets on net basis
- Omission to report comparative figures of the previous year relating to opening balance of fixed assets, addition of fixed assets, depreciation charged for each class of assets

## Instances of non-compliance with Schedule III (2/3)

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- Non-classification of investments into Trade and other investments. Further, it is noted that classification is done incorrectly between Trade and other investments
- Classification of Long-term investments as non-current investments invariably
- Classification of Capital advances paid under capital work-in-progress
- Omission to sub-classify long-term loans and advances into secured considered good, unsecured considered good and doubtful, indicating their degree of realisability



## Instances of non-compliance with Schedule III (2/3)

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- Error in classification of trade receivables, considering the date when they become due for payments
- Error in classification of 'term deposits' under Cash and cash equivalent, other bank balances and other non-current assets
- Disclosure of loans and advances given to related parties without stating any details thereof.

## Instances of non-compliance with Schedule III (2/3)

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- Classification of assets in the nature of 'loans and advances' as 'other current assets', such as, advance tax, MAT credit entitlement, etc.
- Non-disclosure of Uncalled liability of shares and other investments partly paid.
- Omission of disclosure of dividend per share distributed
- Incomplete disclosure of details related to delay payment to MSME. If all the disclosures required stand at Nil, the fact is not disclosed

## Instances of non-compliance with Schedule III (3/3)

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- Non-disclosure of guarantees given by KMPs of the company on behalf of the company as related party transactions
- Book overdraft in current account is netted off with Bank balances
- Consumption of intermediates and components which are internally manufactured are included in 'Cost of material consumed'

Thank You

