Observations of FRRB

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Topics covered

Standard No	Name
AS 1	Disclosure of Accounting Policies
AS 22	Taxes on Income
AS 18	Related Party Disclosure
AS 2	Inventories
AS 3	Cash Flow Statement
AS 15	Retirement Benefits
AS 9	Revenue Recognition
AS 5	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
AS 11	The Effects of Changes in Foreign Exchange Rates
AS 20	Earnings Per Share
Audit Report	CARO Reporting

Improper Accounting Policy

BS

- Impairment losses, if any, on FA are recognized in accordance with the AS 28 and charged to P&L Account
- Intangible assets are recognized in accordance with AS 26
- Deferred tax assets / liabilities have been provided for in the books of accounts in accordance with AS 22
- In case of non member of the Gratuity Fund, the gratuity is provided as per the approval of Central Government and as per the Payment of Gratuity Act 1972, where applicable.

AS – Para 11

- The accounting policies refer to the specific accounting principles and the methods of applying those principles adopted by the enterprise in the preparation and presentation of financial statements

FRRB

- Accounting policy should clearly speak about the:
  - Accounting principles used for recognition and measurement of relevant item
  - Methods as to how such principles have been applied at the time of preparation and presentation of the financial statement.
- Mere reference to the AS cannot be considered as a complete accounting policy

No Accounting Policy disclosed

Company Presentation

- Out of 2 business activities, revenue recognition policy was stated only for 1 business activity
- Significant MAT credit entitlement has been recognized with corresponding recognition of related assets under Long term loans and advances, but no policy for recognition of MAT credit has been disclosed
- No accounting policy disclosed for:

  Fixed Assets, Inventories, Provisions & Contingent Liabilities, Impairment of Assets, Accounting for Taxes on Income, Revenue Recognition, Lease, Employee Benefits, Foreign Currency Transactions, Borrowing Costs, Intangible Assets, Interest, Commission, Royalty

Para 24 of AS 1

- All significant accounting policies adopted in the preparation and presentation of financial statements should be disclosed

Placement of Disclosure of Accounting Policy

Company Presentation

- Certain accounting policies have been disclosed by the enterprises under the heading 'Significant Accounting Policies, however, accounting policies pertaining to Other Items / Transactions have been disclosed by way of notes to various places in the financial statements

Para 25 of AS 1

- The disclosure of the significant accounting policies as such should form part of the financial statements and the significant accounting policies should normally be disclosed at one place.

Offsetting of DTA and DTL in CFS

Company Presentation

- Company having several Subsidiaries disclosed DTA (Net) in the CFS

Para 29 of AS 22

An enterprise should offset DTA and DTL if:

- The enterprise has a legally enforceable right to set off assets against liabilities representing current tax and
- DTA / DTL relate to taxes on income levied by the same governing taxation laws

Observation of FRRB

- In CFS DTA of one enterprise cannot be adjusted against DTL of another enterprise as there is no legal enforceable right to set off

Presentation of DTA and DTL in BS

Company Presentation

- DTL as part of Loan Fund
- DTL as part of Note on Provision
- DTA as part of Current Asset
- DTL after Shareholders Fund
- DTL after the head Net Current Asset as a deduction
- Deferred Tax (net) after Net Current Asset

Para 30 of AS 22

- DTA is disclosed in the BS after the head “Investments” and DTL (net of DTA, if any) after the head “Unsecured Loans”

Non-disclosure of major components of DTA / DTL

Company Presentation

- Break up only for DTA and DTL that have been recognized in Statement of Profit and Loss

Para 31 of AS 22

- The break up of DTA and DTL into major components of the respective balances should be disclosed in the notes to accounts

Non recognition of DTA / DTL in case of Losses

BS

- Due to losses provision for DTA / DTL has not been made
- Note on FA shows Depreciation has been provided during the year

AS – Para 13

- Deferred Tax to be recognized for all timing difference subject to prudence in respect of DTA

FRRB

- Deferred Tax should be recognized for all timing difference
- DTL recognized at BS date give rise to future taxable income at the time of reversal
- DTA to the extent of DTL should be recognized
- Co to recognize DTL on timing difference related to Depreciation and therefore, DTA to the extent of DTL

Virtual Certainty is not supported by convincing evidence

BS

- DTA is recognized only if there is virtual certainty supported by convincing evidence that such DTA can realized against future taxable profits
- Notes – based on the future profitability projections the Company is virtually certain that there would be sufficient taxable income in future, to claim the above tax credit

AS – Para 17

- Virtual certainty refers to the extent of certainty which for all practical purposes can be considered certain.
- Virtual certainty cannot be based on forecasts of performance such as Business Plan
- Virtual certainty is a matter of perception, to be supported by convincing evidence
- Evidence is a matter of fact
- Evidence should be available at the reporting date in a concrete form

FRRB

- Projection of the future profits made by an enterprise cannot, in isolation, be considered as convincing evidence

Non-Disclosure of description of relationship

BS

- Non-Disclosure of description of relationship with Related Parties

Para 23(ii) of AS 18

If there have been transactions between related parties, during the existence of a related party relationship, the reporting enterprise should disclose:

- (ii) a description of the relationship between the parties

Observation of FRRB

- Name as well as transactions with related parties have been disclosed but the nature of relationship with them has not been disclosed
- The phrase “Other Related Parties” has been used rather than giving specific relationship details for the parties with whom transaction has taken place.

Above disclosure does not comply to AS 18

Non-disclosure of certain Related Parties

Company Presentation

- Certain companies are subsidiaries of the other Companies, however name of the Holding Companies have not been disclosed
- Wholly owned subsidiary has been formed during the year, however name of the subsidiary has not been disclosed as related party

Para 21 of AS 18

- Name of the related party and nature of related party relationship **where control exists** should be disclosed irrespective of whether or not there have been transactions between the related parties

Non-disclosure of Related Parties Transactions

BS	AS 18 Para 23	FRRB
▪ Advances given to directors ▪ Application money received from KMP for preferential allotment ▪ Equity shares allotted to KMP ▪ Short term loans given to RP ▪ Remuneration paid to directors (KMP) None of the above disclosed in Related Party Disclosures	In case of transactions between related parties during the existence of the related party relations, disclose: ▪ Name of the RP ▪ Description of the relation ▪ Volume of the transaction in Amount or %, as appropriate ▪ Other element necessary ▪ Amount or % outstanding, provision for doubtful debts due from such parties ▪ Amounts written off or written back	When transactions with Related Parties were disclosed in Notes to Accounts, Cash Flow Statement, Directors Report, Corporate Governance Report, disclosure should have been made in the Related Parties Transactions also for all the transactions taken place during the existence of the related party relationship.

Non compliances relating to KMP

BS	AS 18 Para 14	FRRB
▪ Managing Director, Whole Time Directors, Managers have not been identified as KMP and remuneration paid to them not disclosed under RPD ▪ COO was reported as KMP but not the CEO ▪ Remuneration to KMP has not been disclosed; instead only a reference to the note on managerial remuneration has been given.	▪ KMP are those persons who have the authority and responsibility for: ○ Planning ○ Directing ○ Controlling the activities of the reporting enterprise ▪ In case of a Company Managing Director, Whole Time Director, Manager and any person in accordance with whose directions or instructions the BoD of the Company is accustomed to act are usually considered as KMP	▪ When COO is identified as KMP, CEO is also KMP as he appears to have the authority and responsibility for planning, directing and controlling the activities of the Company ▪ Disclosure made by the Company pursuant to AS 18 with regard to KMP have not been complied with

Incorrect disclosure of valuation of Inventories

BS	AS 2	FRRB
▪ Stocks of Cards are valued at Cost and on FIFO basis and include all applicable overheads in bringing the inventories to their present location and condition. ▪ WIP is valued at cost ▪ Inventories are measured at cost and cost is determined on weighted average basis ▪ WIP is valued at direct RM cost and appropriate cost of completed process ▪ RM are valued at average cost. RM at bonded warehouse, stores, spares, consumables are valued at cost ▪ WIP is valued at RM Cost ▪ Inventories are valued at lower of cost or NRV. Cost is determined by using FIFO. Cost comprises all. ▪ RM are valued at average cost	▪ Para 5 – Inventories should be valued at the lower of cost and NRV ▪ Para 3.2 – NRV is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale ▪ Para 6 – the cost of inventories should comprise all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition	▪ Inventories have been valued at cost or average cost. In other words NRV has not been considered for the purpose of valuation of these inventories. ▪ It is not clear in some of the cases whether all the applicable costs as per Para 6 have been considered or not

Incorrect disclosure of cost formula of Inventories

Company Presentation

- Inventories are stated at lower of cost and NRV. Cost is determined on weighted average / FIFO basis
- Cost of inventories is computed on weighted average / FIFO basis

AS 2

- Para 16 – The cost of inventories should be assigned by using FIFO or weighted average cost formula. The formula used should reflect the fairest possible approximation to the cost incurred in bringing the items of inventory to their present location and conditions
- Para 26 – The financial statements should disclose the accounting policies adopted in measuring the inventories, including the cost formula used

Observation of FRRB

- Though cost formula has been given, it would be more appropriate to disclose which cost formula has been used for which class of inventories

Non adjustment of Unrealized Foreign Exchange Gain / loss

Company Presentation

- In Admin and Other Expenses there is an item of Exchange Fluctuation (net), however, same has not been adjusted to determine the cash flows from operating activities

AS 3 – Para 27

- Unrealized gains and losses arising from changes in foreign exchange rates are not cash flows. However, the effect of exchange rate changes on cash and cash equivalents held or due in foreign currency is reported in cash flow statement in order to reconcile cash and cash equivalents at the beginning and end of the period. This amount is presented separately from cash flows from operating, investing, and financing activities and includes the differences, if any, had those cash flows been reported at the end of the period exchange rates.

Observation of FRRB

- Entire amount cannot be considered to comprise of only realized foreign exchange gain / loss unless such information has been provided. Hence, unrealized foreign exchange gain / loss should have been adjusted to determine the cash flows from operating activities

Interest expense has been reported as net figure in CFS

Company Presentation

- In the Cash Flow Statement of a non-financial enterprise, under the heading financing activities, an item Interest (net) has been reported

AS 3 – Para 30

- Cash flows from interest and dividends received and paid should each be disclosed separately. Cash flows arising from interest paid and dividends received in the case of a financial enterprise should be classified as cash flows arising from operating activities.
- In the case of other enterprises, cash flows arising from interest paid should be classified as cash flows from financing activities while interest and dividends received should be classified as cash flows from investing activities. Dividends paid should be classified as cash flows from financing activities.

Observation of FRRB

- It has been noted that the cash flow arising due to interest expenses has been reported at net figures which indicate that cash flow arising as interest income may have been netted off against the interest expenses. It was viewed that the cash flows from interest income has arisen due to investing activity while the cash flows from interest expense has arisen due to financing activity, hence they cannot be netted off against each other.

Incorrect disclosure of Dividend Tax in CFS

Company Presentation

- Certain companies although are disclosing dividend paid under the heading 'Cash Flow from Financing Activities', have disclosed 'tax on dividend paid (corporate dividend tax)' under the heading 'Cash Flow from Operating Activities

AS 3 – Para 30

- Para 34 - Cash flows arising from taxes on income should be separately disclosed and should be classified as cash flows from operating activities unless they can be specifically identified with financing and investing activities."
- Para 35 - While tax expenses may be readily identifiable with investing or financing activities, the related tax cash flows are often impracticable to identify and may arise in a different period from the cash flows of that underlying transactions. Therefore, taxes paid are usually classified as cash flows from operating activities. However, when it is practicable to identify the tax cash flow with an individual transaction that gives rise to cash flows that are classified as investing or financing activities, the tax cash flow is classified as an investing or financing activity as appropriate.

Observation of FRRB

- Tax on dividend paid (corporate dividend tax) should be shown along with the dividend paid in the Cash Flow Statement under the 'Cash Flow from Financing Activities'. It is not correct to show this amount as 'Cash Flow from Operating Activities' while dividend paid is disclosed as 'Cash Flow from Financing Activities'. It is not in line with the requirements of AS 3

Exclusion of earmarked funds, unpaid dividend

Company Presentation

- The components of Cash and Cash equivalents as reported in the balance sheet includes Cash in Hand, Cash at Bank, Earmarked Balance against LC, Gratuity & Superannuation etc., Unpaid Dividend Account and the total of these components matches with the closing cash & cash equivalents as reported in the cash flow statement.

AS 3 – Para 5.2

- Cash equivalents are short term, highly liquid investments that are readily convertible into known amounts of cash and which are subjects to an insignificant risk of changes in values

Observation of FRRB

- It was observed that the balance of 'Cash and cash equivalents' as reported in the Cash Flow Statement is same as that in the balance sheet i.e. Rs. XXX. Further, it was noted from the components of cash and cash equivalents that it includes balances of unpaid dividend and earmarked balances against LC, Gratuity & Superannuation etc. which are not readily available with the enterprise for its use, thus, the same cannot be included in 'Cash and Cash Equivalents'. Accordingly, it was viewed that the requirement of AS 3 has not been complied with

classification and presentation LT loans / advances

Company Presentation

- In one of the non-financial enterprise, Decrease/ (Increase) in long term loans and advances has been adjusted as working capital changes under the head 'cash flow from operating activity.'
- Further, the cash flows arising from the same have been shown on net basis in the Cash Flow Statement

AS 3

- Para 15 (e) / (f) The separate disclosure of cash flows arising from investing activities is important because the cash flows represent the extent to which expenditures have been made for resources intended to generate future income and cash flows. Examples of cash flows from investing activities are(e) cash advances and loans made to third parties (other than advances and loans made by a financial enterprise); (f) cash receipts from the repayment of advances and loans made to third parties (other than advances and loans of a financial enterprise)
- Para 21 - An enterprise should report separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities, except to the extent that cash flows described in paragraph 22 and 24 are reported on a net basis.

Observation of FRRB

- Decrease/ (Increase) in long term loans and advances has been adjusted as working capital changes under the head 'cash flow from operating activity.' It was viewed that cash flow from operating activities signify cash flows primarily occurring due to principal revenue generating activities of the enterprise. However, for a non-financial enterprise, long term loans and advances are in the nature of investing activity and it cannot be considered as a part of revenue generating activities. Therefore, such cash flows should not be shown under the head 'cash flow from operating activities'.
- Further, it was also noted that such cash lows have been shown on net basis. It was viewed that separate figures of gross receipts and repayments of long term loans and advances, should have been shown

Non provision of Gratuity

Company Presentation

- None of the employees have completed five years, hence gratuity has not been provided.

AS 15

- Matching Concept: All costs relating to financial period should be recognized in the books when related revenue is recognized.

Observation of FRRB

- The company ought to create a provision for gratuity liability irrespective of the fact that none of the employee has completed the mandatory period of five years. It was viewed that the employee's right to receive the benefit is conditional on future employment for a period of five years. Although there is a possibility that the benefit may not vest, there is also a probability that the employee would serve for the minimum period of five years and become eligible for gratuity. Under matching concept an obligation exists even if a benefit is not vested. **The obligation arises when the employee renders the service** though the benefit is not vested. The measurement of this obligation at its present value takes into account the probability that the benefit may not vested and this is appropriately factored in the calculation of the present value of the defined benefit obligation.

Inadequate Disclosure in policy

Company Presentation

- Defined Contribution Plan: Liability for superannuation fund on the basis of premium paid to insurance company in respect of employees covered under superannuation Fund Policy

AS 15 – Para 45 (a)

- When an employee has rendered service to an enterprise during a period, the enterprise should recognize the contribution payable to a defined contribution plan in exchange for that service: (a) as a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the balance sheet date, an enterprise should recognize that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund

Observation of FRRB

- It was observed that the liability for superannuation fund was being provided for on the basis of premium paid to insurance company. However, it had not been disclosed as to whether the said premium is the appropriate accrual of the liability for the year or not. The company had also not indicated as to whether the scheme covers all past as well as present liabilities or it covers only the present liability for the current year. It was felt that in the absence of specific mention to this effect, one may conclude that the scheme does not cover past liabilities and / or that the premium charged is not the appropriate accrual of the liability. Therefore, if that being the case, the company ought to create a provision for past liability in the books and/ or additional liability for the year, as appropriate.

Non / Inadequate Disclosure – Para 120

Company Presentation

- although the company has recognized the defined benefits obligations in the financial statement, however, disclosures required under paragraph 120(a) to 120(o) of AS 15 were not made. "Accounting Policy on Retirement Benefits of one of the company read as follows:
  - Employee Benefits: a. Liability for Gratuity: Company's liability towards Gratuity in respect of employees is worked out on actuarial basis. The total liability as on 31.03.20XX is ` 150.77 lakhs. Out of which ` 54.38 lakhs has been funded and balance ` 96.39 lakhs is yet to be funded.
  - Contributions to Provident Fund are made as per the provisions of Employees' Provident Funds and Miscellaneous Provisions Act, 1952 and remitted to the provident Fund Commissioner

AS 15 – Para 120

- If the employer provides retirement benefit viz. gratuity to its employees then the company is required to disclose certain information as specified under paragraph 120 (a) to (o)

Observation of FRRB

- It was observed from the accounting policy relating to gratuity for employees that the company is providing benefits in the nature of defined benefits plans, accordingly, it was viewed that the disclosures requirements prescribed under paragraph 120 of AS 15 should have been complied with in context of both liabilities for gratuity. However, it was observed from Notes to Accounts that no disclosures have been made with regard to the same

Non Disclosure – Para 47

Company Presentation

- In many of the instances the amount of expense for defined contribution were not disclosed by the enterprises.

AS 15 – Para 47

- An enterprise should disclose the amount recognized as an expense for defined contribution plan.

Observation of FRRB

- It was viewed that since paragraph 47 explicitly requires the disclosure of amount recognized as an expense for defined contribution plan, the same should be shown in the financial statements making appropriate disclosures.

Inadequate Disclosure – Para 65

Company Presentation

- Although the accounting policy on employee benefits stated that defined benefit obligations has been determined using the services of qualified actuary, however, no disclosure was made regarding whether the projected unit credit method was followed in determination of defined benefit obligations or not

AS 15 – Para 65

- An enterprise should use the Projected Unit Credit Method to determine the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost

Observation of FRRB

- it was viewed that enterprises should be encouraged to give appropriate disclosures in the financial statement so as to enable the readers to understand that projected unit credit methods was followed for determining the defined benefits obligations

Recognition of Revenue on Receipt basis

Company Presentation	AS 9 – Para 12	Observation of FRRB
▪ Revenue from sale of tickets is recognized when the tickets have been sold. Advertisement revenue is recognized when advertisements and net realization are confirmed.	▪ In a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method, whichever relates the revenue to the work accomplished. Such performance should be regarded as being achieved when no significant uncertainty exists regarding the amount of the consideration that will be derived from rendering the service.	▪ It was noted that the enterprise under review render services. Therefore, revenue from sale of tickets should be recognized as per the completed contract method. In case of advance booking of tickets there is always a time gap between the sale of tickets and actual event. Hence, such revenue cannot be considered to have been earned until and unless the event has taken place. If the event doesn't take place, it may be necessary even to refund the amount. ▪ The revenue from advertisements should be recognized when the advertisements is accepted and not on realization of bills. Thus, recognizing revenue when advertisement and net realizations are confirmed is not in line with the requirements of AS 9

Timing of Revenue Recognition Insurance claim

Company Presentation

- The company has recognized as income the entire cost of garments destroyed by fire under other operating income (stock loss claim) based on filing of insurance claim. With regard to partially damaged stocks, the related inventory has been valued at net realizable value, and insurance claim against the same is taken as other income. Insurance claim against loss of fixed assets has also been recognized based on the claim filed with the insurance company. The note further states that said income has been recognized as per the AS 9.

AS 9

- Para 4.1 - Revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, rendering of services, and from use by others of enterprise resources….
- Para 9.2 – Where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, e.g., for escalation of price, export incentives, interest etc., revenue recognition is postponed to the extent of uncertainty involved. In such cases, it may be appropriate to recognize revenue only when it is reasonably certain that the ultimate collection will be made. Where there is no uncertainty as to ultimate collection, revenue is recognized at the time of sale or rendering of service even though payments are made by instalments

Observation of FRRB

- it was viewed that as in the case of sale of goods or rendering of services, the recognition of insurance claims also requires that the amount realizable is measurable and it is not unreasonable to expect ultimate collection. Accordingly, recognizing insurance claims at the time of filing the claims with the insurance company without considering the uncertainty relating to its measurability is not appropriate.

Recognition of Dividend Income when right to receive payment is established

Company Presentation

- Dividend is accounted as and when received.
- Income & Expenditures are recognized on accrual basis except dividend on shares and units of Mutual Funds, which are recognized on cash basis.

AS 9 – Para 13

- Revenue arising from the use by others of enterprise resources yielding interest, royalties and dividends should only be recognized when no significant uncertainty as to measurability or collectability exists.
- Dividends from investments in shares: when the owner's right to receive payment is established

Timing of Recognition of Revenue

Company Presentation

- Revenue (income) is recognized when no significant uncertainty as to measurability or collectability exists.
- Revenue/Income and Cost/Expenditure are accounted for on accrual basis.
- Sales are accounted for on dispatch of products.

AS 9 – Para 11

In a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods."

Observation of FRRB

- It was observed in the fist case that revenue has been recognized when there is no uncertainty as to measurability and collectability whereas in the second case it simply states accrual basis. However, in none of these cases the timing of recognition of revenue i.e. when the enterprise has transferred significant risk and reward to the buyer has been disclosed.
- In the last case also, it was not clear whether significant risk and rewards associated with the ownership of goods stands transferred when the products are dispatched.

Expenditure debited to Reserves & Surplus

Company Presentation

From the Annual Reports of some companies, it has been noted that the following items of expenditure have been directly debited to Reserves and Surplus:

- Short provision for Bonus
- Provision for Income Tax relating to earlier years
- Investment Written Off

AS 5 – Para 5

- All the items of income and expense which are recognized in a period should be included in the determination of net profit or loss for the period unless an Accounting Standard requires or permits otherwise."

Observation of FRRB

- It was noted that short provision for bonus and provision for income tax relating to earlier years have been directly debited to Reserves and Surplus. Such liability may have arisen either as a result of error/omissions in the preparation of financial statements of one or more prior periods or that there were circumstances in the current period that have determined the liability in the current period though related to previous period.

- It was viewed that in either case, these expenses should be included in determination of profit or loss of the current period. Similarly, investment written off is also an expenditure of the current period.

Non-disclosure of nature of Prior Period Items

Company Presentation

- Prior period Income – shown under Other Income.
- Prior period expenses – shown in Profit and Loss Account.
- Prior period adjustments (Net) – shown below Profit after Tax

AS 5 – Para 15

- The nature and amount of prior period items should be separately disclosed in the statement of profit and loss in a manner that their impact on the current profit or loss can be perceived.

Wrong Disclosure in Prior Period Adjustments

Company Presentation

- In the Annual Report of a company, 'Sundry Balances written-off' has been disclosed as prior period adjustment.

AS 5 – Para 4.3

- Prior period items are income or expenses which arise in the current period as a result of errors or omissions in the preparation of the financial statements of one or more prior periods

Observation of FRRB

- It was viewed that sundry balances recognized in prior years but written-off in the current year should not be considered as prior period item because such writing-off has not arisen due to any error or omission in preparation of financial statements of prior period/s.
- In fact there has been a change in estimate or change in circumstances due to which company has decided to write-off these balances in the current year.

Wrong Presentation in Exceptional Items

Company Presentation

Following items of income/ expenses have been disclosed in the Statement of Profit and Loss as exceptional items:

- Gain on Finance Lease Arrangement
- Write back of compensation under employee stock option scheme
- Foreign Currency Translation Reserve written off
- Foreign Exchange Fluctuation Difference
- Gain on payment of FCCB
- Tax impact on credit/charge in respect of exceptional items

AS 5

- Para 4.1 - Ordinary activities are any activities which are undertaken by an enterprise as part of its business and such related activities in which the enterprise engages in furtherance of, incidental to, or arising from, these activities.
- Para 12 - When items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately as Exception Items
- Para 4.3 of AS 22 - Tax expense (tax saving) is the aggregate of current tax and deferred tax charged or credited to the statement of profit and loss for the period

Observation of FRRB

- It was observed that the transactions referred to in these cases have arisen from ordinary activities of the enterprises. Further, the size of these transactions does not warrant their classification as 'exceptional items'.

- It was further noted that in one case income tax has been separately deducted under the head 'exceptional items'. In other words, its impact is not considered in the profit/ loss of the year when current tax and deferred tax for the period are measured and recognized. It was viewed that the tax impact of these items should be included as tax expense in the Statement of Profit and Loss

No disclosure of Foreign Exchange gain / loss

Company Presentation

- From Notes to Accounts it is found that certain foreign exchange transactions have been entered during the year
- However, no exchange gain / loss arising on account of foreign exchange fluctuation has been disclosed separately in the Statement of Profit and Loss or in Notes to Accounts.

AS 11 – Para 40(a)

- An Enterprise should disclose the amount of exchange differences included in the net profit or loss of the period

Incorrect valuation of export sales

Company Presentation

- From the accounting policy it was noted that the export sales have been recorded at the rate notified by the customs for invoice purposes

AS 11 – Para 9

- Foreign currency transaction should be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction

Incorrect policy for translation of non-monetary items

Company Presentation

- Current assets and liabilities as at the year end are translated at exchange rate ruling on the date of Balance Sheet

AS 11 – Para 11

- At each Balance Sheet date (a) foreign currency monetary items should be reported using the closing rate..
- Only monetary items are required to be translated at the year end rate and not all the foreign currency assets and liabilities which may include non-monetary assets / liabilities as well

Incorrect policy for translation of monetary items

Company Presentation

- Foreign currency monetary items have been recognized at contracted rate, as those are covered by forward contracts

FRRB

- Hedging contracts (ie forward contracts) are independent of underlying contracts and therefore, both these contracts should be recognized independent of each other
- Monetary items should have been recognized at the closing exchange rate irrespective of the fact whether risk against such items have been hedged by forward contracts

Disclosure of Diluted EPS was sated as Not Applicable

Company Presentation

- Diluted Earnings per Share has been stated as Not Applicable

AS 20 – Para 26, 41

- If Company has no potential equity shares then its diluted EPS would be the same as basic EPS
- In case potential equity shares have an anti dilutive effect, then such potential equity shares are ignored for calculating diluted EPS which will also result in diluted Earnings per Share being equal to basic EPS

Non-disclosure of the types of EPS

Company Presentation

On the face of the profit and loss as well as under notes to accounts, only ‘earning per share’ has been disclosed

AS 20 – Para 8

Even if there is no difference in the basic and diluted EPS, to comply with AS 20, the basic as well as diluted EPS should be explicitly disclosed.

Merely stating ‘earning per share’ is not in compliance to AS 20

Non-disclosure of nominal value of shares

Company Presentation

In the Statement of Profit and Loss as well as Notes to Accounts, the nominal value of shares was not disclosed

AS 20 – Para 48

In addition to disclosures as required by Para 8,9 and 44, an Enterprise should also disclose..
(ii)(c) the nominal value of shares along with the earnings per share figures

Incorrect calculation of weighted average number of shares

Company Presentation

- From the details given in the Annual Report it was noted that number of equity shares outstanding during the year has increased as on balance sheet date compared to last balance sheet date
- Director's Report states that shares have been issued during the year
- For computing basic EPS number of shares outstanding on the balance sheet date has been considered

AS 20 – Para 15

- For the purpose of calculating basic EPS, the number of equity shares should be weighted average number of equity shares outstanding during the period
- Weighted average number of shares would be different from the outstanding number of shares as there is an increase in the number of shares during the year

Share Application Money not considered for computing diluted EPS

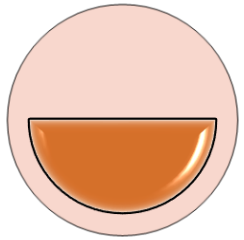
Company Presentation

- Share application money received was disclosed in the Balance Sheet of the Company
- Basic EPS and Diluted EPS have been disclosed at the same value

AS 20 – Para 28, 32

- Share application money pending allotment as at the balance sheet date, which is not statutorily required to be kept separately and is being utilized in the business of the enterprise, is treated in the same manner as dilutive potential equity shares for the purpose of calculation of diluted EPS
- Potential equity shares arising due to share application money pending allotment needs to be considered for calculating diluted EPS

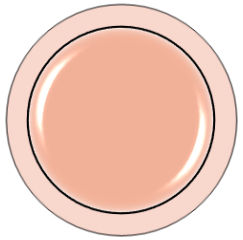
Incorrect disclosure of EPS



Company Presentation

In the Annual Report of a Company basic and diluted EPS has been reported as Nil

It was noticed from the Statement of Profit and Loss that Company has incurred loss during the year



AS 20 – Para 9

An enterprise to present basic and diluted earnings per share, even if the amounts disclosed are negative (a loss per share)

Clause 3(i)(a) – Fixed Assets Records

Auditors Presentation

- The Company has maintained reasonable records showing full particulars, including quantitative details and situation of fixed assets.
- The Company has generally maintained proper records showing full particulars including quantitative details and situation of fixed assets

Observation of FRRB

- In the first case it was noted by the Board that auditor has reported on maintenance of 'reasonable records' instead of 'proper records'. It was viewed that the use of words such as 'reasonable records' gives the impression of impromper reporting by the auditor and does not clearly indicate whether proper records have been maintained by the company or not.
- Similarly, in second case it was viewed that usage of term 'generally maintained' gives the impression that there might be the instances where proper records of fixed assets have not been maintained by the company for some of the asset classes. If such being the case, auditor is obligated to report the deficiencies in record maintenance

Clause 3(i)(b) – Fixed Assets Records

Auditors Presentation

- As explained to us, fixed assets are physically verified by the management at reasonable intervals in a phased manner in accordance with a program of physical verification. We are informed that no material discrepancies were noticed on such verification
- The management, at the end of the year, has physically verified the fixed assets and we have been informed that no material discrepancies were noticed
- Physical verification of the fixed assets is covered under a scheme of verification over a period of three years. No serious discrepancy was noticed on such verification during the period

Observation of FRRB

- It was viewed that use of the words 'we are/ have been informed' or 'as informed …'or 'as explained to us' or 'as certified to us' indicates that auditor has not carried out adequate audit procedure to satisfy himself regarding the reasonableness of verification procedure of fixed assets as well as in determination of materiality of the discrepancies observed in the management's verification of fixed assets.
- It gives the impression that auditor has solely relied on the assertions made by the management. It may be noted that sub-paragraphs (c), (e) and (f) of paragraph 35 of Guidance Note on CARO, 2016 cast the duty on auditor to examine reasonableness of the method of verification of fixed assets, reasonableness of intervals of the verification and whether the material discrepancies were noticed on such verification.

Clause 3(i)(c) – Verification of Title Documents

Auditors Presentation

- Although auditor has commented on requirements of paragraph 3(i)(a) and 3(i)(b) however, he did not comment on title deeds of immovable properties as required under paragraph 3(i)(c) of the Order, at all.
- In some cases, it was observed that although auditors has reported that in case of certain immovable properties title deeds were not held in the name of the company, however, omitted to give details of such properties

Observation of FRRB

- Incomplete reporting has been done by the auditor as it does not comply with the requirements of clause 3(i)(c) of the Order.

Clause 3(ii) – Verification of Inventories

Auditors Presentation

- Inventories have been physically verified by the management. According to the information & explanations given to us, no discrepancies were noticed on physical verification of inventories.
- As explained to us, the inventories of the company at all its locations (except stock lying with third parties and stock-in-transit) have been physically verified by the management at reasonable intervals and no discrepancies were found.

Observation of FRRB

- In first case, it was observed that although auditor has reported that physical verification has been done by the management, however, he omitted to report whether such verification of inventories was done at reasonable intervals or not. It was viewed that paragraph 37(d) of Guidance Note on CARO, 2016 casts the duty upon the auditor to satisfy himself that physical verification of inventories has been conducted at reasonable intervals.
- In second case, it was viewed that the comment of auditor gives an impression that stock lying with third parties and stock-in-transit are material items and therefore adequate audit procedure need to be followed for such stock also. Further, use of term 'as explained to us' indicates that the auditor has simply relied on the explanation of the management rather than using his own judgment, backed by the adequate audit procedures, in forming opinion about no discrepancies being observed in the physical verification of inventories

Clause 3(iii) – Loans and Advances to RP

Auditors Presentation

- "According to the information and explanation provided to us and as per the records examined by us, as at 31st March, 20xx, company has granted interest free unsecured loans amounting Rs. xxx to two of the parties covered in the register maintained under section 189 of Companies Act, 2013. Maximum balance outstanding during the year amounted to ` xxx. In our opinion, terms and conditions of such loan are prima facie not prejudicial to the interest of the company

- To the best of our knowledge and as per our verification of the books and records, the company has neither provided any guarantee nor granted any loan to companies, firms and other parties covered under section 189 of the Companies Act 2013

Observation of FRRB

- In first case it was viewed that although auditor has reported that interest free loan has been provided to two of the parties covered under section 189 of Companies Act, 2013 as well as the terms and conditions of such loans as required under clause 3(iii) (a) of CARO, 2016. However, auditor omitted to comment on the requirements of sub-clause (b), and (c) of clause 3(iii) of CARO, 2016 regarding schedule of repayment of principal and overdue amount, if any, for more than ninety days as well as steps regarding recovery of such overdue amount, respectively.

- In second case it was viewed although, auditor has reported on loan given or guarantees provided to companies, firms and other parties covered under section 189, however, he did not include 'Limited Liability Partnership' in his comment

Clause 3(iv) – Compliance to Section 185 / 186

Auditors Presentation

- Auditor commented on investments, guarantees and security however he omitted to cover loans while reporting under clause 3(iv)
- Auditor reported that requirements of Section 186 has been complied with however it was noted from the Notes to Accounts that company had provided interest free loans to its holding company, which is a non-compliance of Section 186(7)

Observation of FRRB

- It was viewed that clause 3(iv) specifically requires auditor to comment on compliance of Section 185and 186 in respect of:
  - loans given
  - investments made
  - guarantees given and
  - security provided.

Non-reporting on any of the item would be a non-compliance of clause 3(iv).

- In second case it was viewed that auditor's reporting was contradictory to the facts presented in the Financial Statement which is not correct.

Clause 3(v) – Acceptance of Deposit

Auditors Presentation

- The Company has not accepted deposits from the public, under the directives issued by the Reserve Bank of India and the provisions of the Section 73 to 76 of the Act and the rules framed thereunder. However, temporary loans have been taken from employee welfare trust without adequate records

Observation of FRRB

- It was noted that under the given clause, the auditor has also reported about inadequate records for temporary loans taken from employee welfare trust. The context due to which such fact was included in the aforesaid clause was not clear. It was viewed that in case those temporary loans fall within purview of Section 73 to 76 of Companies Act, it should have been reported clearly. However, if those loans fall outside the purview of this clause and auditor still wants to draw attention of reader to such facts then it should have been reported as 'Emphasis of Matter' as per SA 706

Clause 3(vii)(a) – Undisputed Statutory Dues

Auditors Presentation

- Undisputed statutory dues including provident fund, income-tax, service-tax, and ESIC have been generally deposited in many cases with the appropriate authorities except that there have been delays in payment of service-tax in few cases

Observation of FRRB

- It was noted that although auditor has commented on regular deposit of income-tax, service-tax and ESIC, however, he omitted from commenting on duty of customs, duty of excise and other statutory dues.

- It was further noted that in case of delay in deposit of service-tax, auditor has not reported the fact in the manner as required under paragraph 42(q) of Guidance Note on CARO, 2016 issued by AASB of ICAI

Clause 3(vii)(b) – Disputed Statutory Dues

Auditors Presentation

- According to the information and explanations given to us, no disputed amount payable in respect of income tax, wealth tax, sales tax, custom duty, excise duty and cess were in arrears, as at 31st March, 20XX for a period of more than six months from the date on which they are payable

Observation of FRRB

- It was viewed that auditor has commented only on those disputed statutory dues which are in arrears for a period of more than six months. It was viewed that paragraph 3(vii)(b) of the Order requires the auditor to report on all disputed statutory dues irrespective of the period of their arrears, unlike in the case of reporting for undisputed statutory dues.

Clause 3(viii) – Default in repayment of Loan

Auditors Presentation

- In many of the cases it was noted that although auditors omitted to include one or more of the lenders in their comments while reporting under this clause.
- In some cases, it was also found that although auditors have reported that there had been defaults in repayment of certain loans however, further details about such defaults have not been reported as required under this clause.

Observation of FRRB

- It was noted that non-inclusion of any of the lending entities while commenting on default in repayment of loans/ borrowings under this clause is an incomplete reporting, auditor shall comment on all the loans/ borrowings taken from banks, financial institutions and Government as well as dues to debenture holders.
- It was further noted that if auditor observes that there have been default in repayments of loans/borrowings/ dues, he should report the details of such default in the manner prescribed under paragraph 44(l) of Guidance Note on CARO

Clause 3(ix) – Use of IPO and other funds

Auditors Presentation

- In many cases it was observed that auditors, while reporting under clause 3(ix) have commented only on money raised by way of initial public offer/ further public offer (IPO/FPO) and skipped to include term loans in their comments
- In some cases, it was also noted that, though the auditor has reported that there have been defaults in utilization of said money on the purpose they were raised for, however, further details of such defaults were not disclosed

Observation of FRRB

- It was noted that clause 3(ix) of the Order specifically requires the auditor to comment on utilization of the monies raised through IPO/FPO as well as through term loans. Omitting any source of fund in the comment will tantamount to incomplete reporting.
- Further, if auditor is of the opinion that there have been defaults in use of the money for the intended purpose, he shall report the details in the manner specified under paragraph 45(s) of Guidance Note on CARO, 2016

Clause 3(x) – Reporting of Fraud

Auditors Presentation

- According to the information and explanations given to us, no fraud on company by its officers or employees has been noticed or reported during the course of audit.
- In our opinion and according to the information and explanations given to us, no fraud on company by its employees or officers has been noticed during the year, that causes the financial statements to be materially misstated

Observation of FRRB

- In first case it was noted that reporting under clause 3(x) is not correct as it indicates that auditor has restricted the scope of the comment under the paragraph to the frauds noticed during the course of his audit which is as required by Section 143 (12) of the Companies Act, whereas clause under 3(x) of CARO requires reporting on any fraud noticed by the company during the year
- In second case it was viewed that auditor has given a conditional statement that if fraud have occurred, they do not materially misstate the financial statement. However, the clause requires that if fraud has occurred, auditor should report the nature and amount involved

Clause 3(xiii) – Transactions with Related Party

Auditors Presentation

- Company has not entered into related party transaction during the year, and therefore, requirements of clause 3(xiii) are not applicable. However, notes to the account disclosed related party transactions. According to the information and explanations given to us, no fraud on company by its officers or employees has been noticed or reported during the course of audit

Observation of FRRB

- It was viewed that reporting done by auditor under clause 3(xiii) is not correct as there have been transactions with related parties and auditor has not carried out adequate procedure to satisfy himself regarding compliance of Section 177 and 188 of Companies Act, 2013 w.r.t. such transactions. It was, further, viewed that if auditor, after adequate audit procedures, comes across any non-compliance of Section 177 and 188 it should be reported in the manner prescribed under clause 49(o) of Guidance Note on CARO, 2016. It was viewed that information reported in the financial statements i.e., Balance Sheet, Statement of Profit & Loss, Cash Flow Statement and notes to accounts should corroborate with the report of auditor be it Statutory audit report, reporting under CARO or on Internal Financial Controls

THANK YOU

WISH YOU A VERY ENJOYABLE AUDITING