Financial Reporting Practices

Schedule III to the Companies Act, 2013, lays down principles for preparation and presentation of balance sheet as well as statement of profit and loss for Indian enterprises for the financial years commencing on or after April 1, 2014. The format prescribed in Schedule III to the Companies Act, 2013 is same as that given in Revised Schedule VI to the Companies Act, 1956, but there is drastic change from pre-revised Schedule VI. Financial Reporting Review Board (FRRB or "the Board") has identified various non-compliances with respect to Revised Schedule VI during its review of the general-purpose financial statements of various enterprises. Through this column, we wish to share with members, both in practice or industry, some such instances specific to Revised Schedule VI, so that they observe the highest level of best practices while complying with reporting obligation under Schedule III to Companies to Companies Act, 2013. In a nutshell, this column aims to empower the professionals in their day-to-day work and thus enhance the overall image of the profession. Members are requested to send their response and contribute.

SHAREHOLDERS' FUNDS

Share Capital

It has been noted that from the balance sheet of certain enterprises that they omit to report one or more of the following disclosures as required under Part I, Revised Schedule VI to the Companies Act, 1956, with respect of Share Capital:

- A reconciliation of the number of shares outstanding at the beginning and at the end of the reporting period.
- The rights, preferences and restrictions attaching to each class of shares.
- Terms of any securities convertible into equity/ preference shares issued, the earliest date of conversion.
- Shares held by the associates of holding company or ultimate holding company.
- Number of shares held by the shareholders holding more than 5% shares.
- Aggregate number and class of shares bought back during last five years immediately preceding the date of the balance sheet.

Omission of any such information is not in accordance with the Revised Schedule VI.

Reserves and Surplus

While Old Schedule VI prescribes to show debit balance of Profit and Loss is in excess of uncommitted reserves on the assets side of the balance sheet, the Revised Schedule VI prescribes to show debit balance of profit and loss as a negative figure which if in excess of uncommitted reserve would be shown as a negative figure under the head 'Surplus'. However, it has been noted that some enterprises continue to follow the old practice of showing the debit balance profit and loss on the assets side. It is against the requirements of Revised Schedule VI.

NON-CURRENT LIABILITIES

Long Term Borrowings

It may be noted that as per Note 6 (C) (vi) of 'General Instructions for preparation of Balance Sheet', Part I, Revised Schedule VI to the Companies Act, 1956,

(Contributed by Financial Reporting Review Board of ICAI. Comments can be sent at frrb@icai.in.)

the repayment terms of term loans as well as other loans are required to be separately disclosed. Thus, disclosure of repayment terms involve following disclosures:

- period of maturity with respect to the Balance Sheet date,
- number and amount of instalments,
- the rate of interest and
- other significant relevant terms, if any.

It has been noted that many enterprises take term loans in the nature of vehicle loans, loans from banks–secured or unsecured or issue bonds and debentures. It has been observed that in some cases, the rate of interest at which such loans have been taken has not been disclosed. In other cases, only the amount of outstanding liability as at the end of the period and the rate of interest have been disclosed, other repayment terms of the loan-the period of maturity, number and amount of installments have not been disclosed. It is a non-compliance of reporting requirements of Revised Schedule VI.

Other Long term Liabilities

Pursuant to the requirements of Note 6 (D) of 'General Instructions for Preparation of Balance Sheet' given under Part I of the Revised Schedule VI to the Companies Act, 1956, Other Long term Liabilities shall be classified as:

"(a) Trade payables

(b) Others"

It has been noted from the balance sheets that many enterprises report substantial amount of long term liabilities under the head 'others' without specifying the nature of such liabilities. It was viewed that the 'others' can be in the nature of trade payable, dues payables in respect of statutory obligations like contribution to provident fund, dues payable against purchase of fixed assets or contractually reimbursable expenses. To enhance the readability of the financial statements, the Revised Schedule VI prescribes to disclose all the important information that may assist the users in understanding the financial statements. Accordingly, it was viewed that different nature of long term liabilities apart from trade payables should be shown separately specifying their nature rather than clubbing them under a common-head 'others'. In latter cases, the requirements of Part I, Revised Schedule VI to the Companies Act, 1956 cannot be considered to have been strictly complied with.

CURRENT LIABILITIES

Pursuant to the requirements of Part I, Revised Schedule VI to the Companies Act, 1956, 'Current liabilities' are sub-classified as prescribed below:

"(4) Current liabilities

(a) Short-term borrowings

(b) Trade payables

(c) Other current liabilities

(d) Short-term provisions"

The following discrepancies have been noticed with regard to presentation of information under the head 'Current liabilities':

Trade Payables

- It was observed that in some financial statements, 'sundry creditors' for goods were shown as separate line item under the head 'current liabilities'. It may be noted that under the Old Schedule VI, 'sundry creditors' were prescribed as a separate line item. However, in Revised Schedule VI the head 'sundry creditors' does not exist, instead there is a head of 'trade payables'. It was viewed that 'trade payables' may arise on account of goods purchased or services received in the normal course of business. Hence, sundry creditors for goods are trade payables which should be shown under the sub-head 'trade payables' instead of the head 'sundry creditors'.
- In other cases, it was noted that under the head trade payables a sub-head 'sundry creditors' has been shown as a separate line item. It may be noted that the head 'sundry creditors' may include dues other than that in the nature of trade payable viz, dues payables in respect of statutory obligations like income tax or other contractual obligations that may not have occurred due to goods purchased or services received in the normal course of business. Thus, the term 'sundry creditors' is wider than the term 'trade payable'. Hence, presentation of sub-head 'sundry creditors' under the broad head 'trade payable' is not a correct presentation of information.

Other Current Liabilities

Under Note 6 (G) of 'General Instructions for preparation of Balance Sheet' given under Part I, Revised Schedule VI to the Companies Act, 1956, 'Other Current Liabilities' is required to be presented in the format as prescribed below:

"(G) Other Current Liabilities

The amounts shall be classified as:

(a) Current maturities of long-term debt;

(b) Current maturities of finance lease obligations;
(c) Interest accrued but not due on borrowings;
(d) Interest accrued and due on borrowings;
(e) Income received in advance;
(f) Unpaid dividends;
(g) Application money received for allotment of securities and due for refund and interest accrued thereon;...
(h) Unpaid matured deposits and interest accrued thereon;
(i) Unpaid matured debentures and interest accrued thereon;
(j) Other payables (specify nature); "

From the above, it may be noted that 'other current liabilities' should either be classified in one of heads as suggested from (a) to (i), in case of other payables, they should be shown separate line item specifying their nature. It was noted, that in many balance sheets the nature of 'other payables' has not been disclosed which is against the aforesaid requirement of Revised Schedule VI to the Companies Act, 1956.

Short-Term Provisions

It has been noted that certain enterprises have shown liabilities towards employee benefits as 'short-term provisions'. It was viewed that employee benefit liabilities measured under AS 15, Employee Benefits, should be bifurcated into current and non-current liabilities. Any liability towards employee benefits payable within a period of 12 months and the enterprise does not have unconditional right to defer its settlement for 12 months after the reporting date, such liabilities should be classified as current and should be shown under the head 'short-term provisions' and remaining liabilities should be sown under the head 'long-term provisions'.

NON-CURRENT ASSETS

1. It may be noted that Part I, Revised Schedule VI to the Companies Act, 1956, prescribes to classify Non-Curent Assets as follows:

   "(1) Non-current assets
   (a) Fixed assets
   (i) Tangible assets
   (ii) Intangible assets
   (iii) Capital work-in-progress
   (iv) Intangible assets under development"

   From the above, it may be noted that Revised Schedule VI prescribes to classify tangible assets not yet ready for use as 'capital work-in-progress' and intangible assets still under development as 'Intangible assets under development'. It has been noted from the accounting policy of Intangible assets that expenses incurred on intangibles under development viz, for acquiring intellectual property rights or licenses for projects that are still under development have been classified as 'capital work-in-progress'. It was viewed that capitalisation of expenses incurred on the intangible assets still under development under the head 'capital work-in-progress' is not in line with the requirements of Part I, Revised Schedule VI to Companies Act, 1956.

2. It may further be noted that as regards presentation of the Non-Current assets, Note I (iii) of 'General Instructions for the preparation of the Balance Sheet' given under Part I, Revised Schedule VI to the Companies Act, 1956, requires that

   "I. Tangible assets
   ...
   (iii) A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations and other adjustments and the related depreciation and impairment losses/reversals shall be disclosed separately."

   It has been noted that, at times, enterprises show Additions/(Deletion) to fixed assets in a single column while their Cash Flow Statements show that during the period cash flows have occurred due to purchasing and selling of fixed assets. It was viewed that figures of additions and deletions in a single column indicate that such figures have been reported on net basis. It was viewed that as per the presentation requirement of non-current assets, additions as well as deletions of fixed assets should be reported separately on the gross basis. In the absence of such information, the gross value of fixed assets purchased and sold cannot be ascertained.

3. Enterprises often omit to report the comparative figures of the previous year relating to opening balance of fixed assets, addition of fixed assets during the year, depreciation charged for each class of fixed assets. Such disclosure is necessary as required under as per paragraph 5 of 'General Instruction for preparation of Balance Sheet

and Statement of Profit and Loss…'given under Revised Schedule VI reproduced below:

> "Except in the case of the first Financial Statements laid before the Company (after its incorporation) the corresponding amounts (comparatives) for the immediately preceding reporting period *for all items shown in the Financial Statements including notes shall also be given (emphasis added)."*

Non-Current Investments

It may be noted that Note 6 (K) of 'General Instructions For Preparation Of Balance Sheet' given under Part I, Revised Schedule VI to the Companies Act, 1956 requires to classify the non-current investments into one or more of the heads prescribed thereunder as reproduced below:

"K. Non-current investments

(i) Non-current investments shall be classified as trade investments and other investments and further classified as:

(a) Investment property;

(b) Investments in Equity Instruments;

(c) Investments in preference shares

(d) Investments in Government or trust securities;

(e) Investments in debentures or bonds;

(f) Investments in Mutual Funds;

(g) Investments in partnership firms

(h) Other non-current investments (specify nature)

…

(iii) The following shall also be disclosed:

(a) Aggregate amount of quoted investments and market value thereof;

…"

1. It has been noted that some enterprises does not correctly classify the investments into trade investments and other investments. At times investments in subsidiaries are classified as 'other investments' and investments in money market are classified as 'trade investments'. It may be noted that 'trade investments' refers to those investments that are made to promote the business of the enterprise. Thus, subsidiaries established to promote the business of the enterprise are its 'trade investments', however, investments in money market are made to earn income by way of dividends /interest or for capital appreciation. In other words, the investments in money market cannot be considered to have been made for promotion of business of the enterprise. Hence, their classification as 'trade investments' is incorrect.

2. It may be noted that whereas AS 13 requires that investments to be classified into long-term and current investments, Revised Schedule VI of Companies Act, 1956 requires to classify the same as non-current and current investments. It has been observed that many enterprises invariably classify their long–term investments into non-current investments. It may be noted that investments which are realisable beyond 12 months from the date of the balance sheet are non-current investments. Thus, the investments are classified into long-term and other investments on the basis of date of their original investment. However, they are classified into non-current and current on the basis of their realisation. Thus, in all cases it may not be necessary that all long-term investments are non-current investments.

3. At times, the investments are simply disclosed as non-current investment without specifying the nature of such investment or the aggregate market value of quoted investments/unquoted investments have not been disclosed separately. Such incomplete information leads to non-compliance of the requirements of Revised Schedule VI to the Companies Act, 1956.

Long-term loans and advances

1. As per Note 6 (L) (i) of 'General Instructions for Preparation of Balance Sheet' given in Part I, Revised Schedule VI to the Companies Act, 1956, 'Long-term loans and advances' comprises of following sub-heads:

   "L. Long-term loans and advances

   (i) Long-term loans and advances shall be classified as:

   (a) Capital Advances;

   (b) Security Deposits;

   (c) Loans and advances to related parties (giving details thereof);

   (d) Other loans and advances (specify nature) *(emphasis added)."*

   It has been noted from the accounting policy of certain enterprises that capital advances paid are included in capital work-in-progress. It was viewed that while capital advances refers to advances paid for acquisition of fixed assets, capital work-in-progress refers to the expenditure incurred on capital assets which are in the process of construction or completion. An advance may be refunded on non-completion of contract but it cannot happen with incomplete capital work-in-progress. Hence, capital advances are not in the nature of capital work-in-progress but over the period they are expected to be converted into fixed assets which are non-current assets. Therefore, capital advances paid should be classified as long-term loans & advances.

2. It may be noted that Note 6 (L) (ii) of 'General Instructions for Preparation of Balance Sheet' given in Part I, Revised Schedule VI to the Companies Act, 1956, requires to sub-classify 'Long-term loans and advances' into secured, considered good; unsecured, considered good and doubtful, thus indicating their degree of realisability. However, many enterprises omit to sub-classify long-term loans and advances accordingly. This is a non-compliance of the Part I, Revised Schedule VI to Companies Act, 1956.

CURRENT ASSETS

Pursuant to the requirements of Part I, Revised Schedule VI to the Companies Act, 1956, 'Current assets' are sub-classified as prescribed below:

"(2) Current assets
(a) Current investments
(b) Inventories
(c) Trade receivables
(d) Cash and cash equivalents
(e) Short-term loans and advances
(f) Other current assets"

Following discrepancies have been noticed with regard to presentation of information under the head 'Current assets':

Trade Receivables

At times, enterprises report trade receivables using the head 'Trade Receivables for a period exceeding six months'. It may be noted that Revised Schedule VI requires under this head disclosure of those trade receivables which are outstanding for a period exceeding six months *from the date when they become due for payment.* However, by using ambiguous heads it is not clear as to whether the trade receivables have been classified based on the date of their original transactions or the date when trade receivables become due for payment. It may be possible that at one point of time a transaction may be a trade receivable but amount may not be due for on it. Hence, trade receivable should be classified considering the time when payments fall due with them for correct presentation under Part I, Revised Schedule VI to Companies Act, 1956.

Cash and cash equivalents

It may be noted that Note 6 (Q) of 'General Instructions for Preparation of Balance Sheet' given in Part I, Revised Schedule VI to the Companies Act, 1956, interalia, provides that:

"Cash and Cash Equivalents
(i) Cash and Cash Equivalents shall be classified as:
(a) Balances with banks;
(b) Cheques, drafts on hand;
(c) Cash on hand;
(d) Others (specify nature).
…
(v) Bank deposits with more than 12 months maturity shall be disclosed separately."

Generally, enterprises do not classify the 'term deposits' correctly. In certain cases, term-deposit with banks with a maturity of more than 12 months are shown as balances with banks under the broad head cash and cash equivalents. In other cases, non-current portion of term-deposits are not disclosed separately. It may be mentioned that there should be a broad head of 'Cash and bank balances' with sub-classifications – 'Cash and cash equivalents' and 'Other bank balances'. The term deposits with *original maturity* of three months or less from the date of acquisition should only be classified as 'cash and cash equivalents' and those with more than three months to 12 months maturity should be classified as 'Other bank balances'. However, the non-current portion of each of the above balances along with term-deposits of more than 12 months maturity should be classified as 'Other Non-current assets' with separate disclosure thereof.

Short-term loans and advances and Other Current Assets

1. As per Note 6 (R) of 'General Instructions For Preparation of Balance Sheet' given under Part I, Revised Schedule VI to the Companies Act,1956 in case of short term loans and advances given to related parties, their details are also required to be disclosed. However, it has been noted that enterprises simply state the aggregate amount of short-term loans and advances given to such

parties without stating any details thereof. It is a non-compliance of the requirements of Revised Schedule VI to the Companies Act, 1956.

2. It has been noted that items in the nature of advances which are recoverable in cash or kind viz., advance tax, MAT credit entitlement, advance excise duty etc are shown under the head 'other current assets'. It may be noted that assets in the nature of 'loans and advances' cannot be classified as 'other current assets'. It is not in line with the requirements of Revised Schedule VI to the Companies Act, 1956.

Other Disclosures

1. Further, it may be noted that Note T (ii) (b) of 'General Instructions for Preparation of Balance Sheet' given in Part I of the Revised Schedule VI to the Companies Act, 1956 requires disclosure of commitments as follows:

   "T.

   (ii) Commitments shall be classified as:

   (a) ...;

   (b) Uncalled liability on shares and other investments partly paid."

   It has been noted that often enterprises holds partly paid investments but omit to report commitments for unpaid investments. It results in non-disclosure of commitments which is against the requirements of Revised Schedule VI to the Companies Act, 1956.

2. Paragraph 6 (U) of 'General instructions for the preparation of Balance Sheet' given under Part I of the Revised Schedule VI to the Companies Act, 1956, lays down the requirements relating to disclosure of proposed dividend which, interalia, states as follows:

   "The amount of dividends proposed to be distributed to equity and preference shareholders for the period and ***the related amount per share*** shall be disclosed separately... (**emphasis added**)"

   It was noted that the total amount of dividend proposed to be distributed to equity shareholders for the period has been disclosed; however, dividend per share distributed has not been disclosed. Accordingly, it was viewed that the requirement of Revised Schedule VI to the Companies Act, 1956 has not been complied with.

3. It may be noted that disclosures relating to delayed payments to Micro, Small and Medium Enterprises although not specifically required under Revised Schedule VI, Section 22 of Micro, Small and Medium Enterprises Development (MSMED) Act, 2006, requires every buyer to give following disclosures in the financial statements wherever, they are audited under any law:

   "Where any buyer is required to get his annual accounts audited under any law for the time being in force, such buyer shall furnish the following additional information in his annual statement of accounts, namely:

   a) the principal amount and the interest due thereon (to be shown separately) remaining unpaid to any supplier as at the end of each accounting year;

   b) the amount of *interest paid by the buyer* in terms of section 18, along with the amounts of the payment made to the supplier beyond the appointed day *during each accounting year;*"

   c) the amount of interest due and payable for the period of delay in making payment (*which have been paid but beyond the appointed day during the year)* but without adding the interest specified under this Act;

   ... (*emphasis added*)"

   Hence, such disclosures should be made in every financial statement. In case if there are no dues as at the end of year, the company is still required to disclose information sought under clause (b) and (c) of section 22 of Micro, Small and Medium Enterprise Development Act, 2006. If all the disclosures required stand at nil, the fact should be disclosed rather than omitting the information relating to micro, small and medium enterprise from the financial statements.

It is pertinent to mention that the requirements relating to preparation and presentation of financial statements under Schedule III to Companies Act, 2013 are nearly same as that of Revised Schedule VI to the Companies Act, 1956. Accordingly, the observations of FRRB made with respect to Revised Schedule VI to Companies Act, 1956 will also be relevant for preparation of financials statements under Schedule III to Companies Act, 2013. However, the members are advised to refer to Schedule III to Companies Act, 2013 before finalising the financial statements. ■