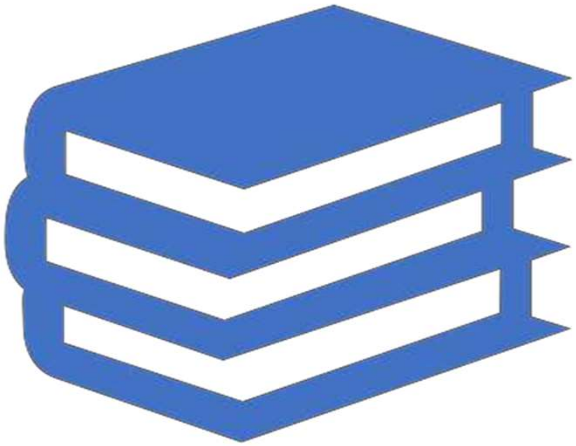
Training Program for PEER REVIEWERS



Compliance with technical & professional standards

PEER REVIEW BOARD OF ICAI

KOLKATTA BRANCH OF EIRC OF ICAI

Objective of Peer Reviewer

To ensure that in carrying out the assurance service assignments, the members of the Institute

(a) comply with Technical, Professional and Ethical Standards as applicable including other regulatory requirements thereto and

(b) have in place proper systems including documentation thereof, to amply demonstrate the quality of the assurance services.

Non-compliance

Practice Units which are found to be deficient in complying with the technical, professional and ethical standards and

Do not have in place proper systems including documentation thereof to amply demonstrate the quality of the assurance services.

Shall be subject to disciplinary proceedings.

Scope of Peer Reviewer

The Peer Review Guidelines lays down the scope of review to be conducted as under:

- The Peer Review process shall apply to all the assurance services provided by a Practice Unit.
- Once a Practice Unit is selected for Review, its assurance engagement records pertaining to the Peer Review Period shall be subjected to Review.

Scope of Peer Reviewer

- The Review shall cover:
  a. **Compliance with Technical, Professional and Ethical Standards**
  b. Quality of reporting
  c. Systems and procedures for carrying out assurance services
  d. Training programmes for staff (including articled and audit assistants) concerned with assurance functions, including the availability of appropriate infrastructure.
  e. Compliance with directions and /or guidelines issued by the Council to the Members, including fees to be charged, number of audits undertaken, register for assurance engagements conducted during the year and such other related records.
  f. Compliance with directions and /or guidelines issued by the Council relating to article assistants and /or audit assistants, including attendance register, work diaries, stipend payments, and such other related records."

Technical, Professional and Ethical Standards?

(i) **Accounting Standards** issued by ICAI that are applicable for entities **other than companies** under the Companies Act,2013;
(ii) **Accounting Standards** prescribed under section 133 of the Companies Act; 2013 by the Central Government based on the recommendation of ICAI and in consultation with the National Financial Reporting Authority (NFRA) and notified as **Accounting Standards Rules 2006,** as amended from to time;
(iii) **Indian Accounting Standards** prescribed under section 133 of the Companies Act 2013 by the Central Government based on the recommendation of ICAI and in consultation with NFRA and notified as **Companies (Indian Accounting Standards) Rules, 2015,** as amended from time to time;

Technical, Professional and Ethical Standards?

(iv) Standards issued by the Institute of Chartered Accountants of India including

(a) Engagement and Quality Control Standards

(b) Statements

(c) Guidance notes

(d) Standards on Internal Audit

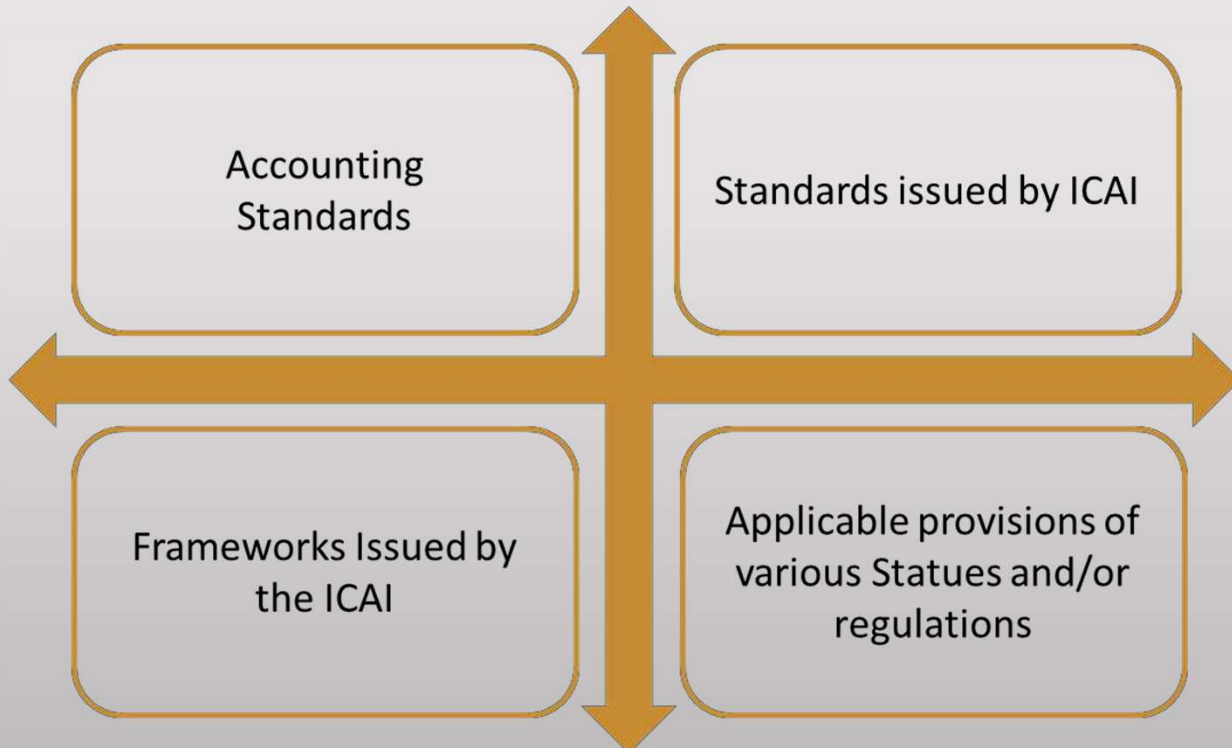
(e) Guidelines/ Notifications / Directions / Announcements / Pronouncements / Professional Standards issued from time to time by the Council or any of its Committees.

(v) Framework for the preparation and presentation of financial statements, Preface to the Standards on Quality Control, Auditing, Review, Other Assurance and Related Services and Framework for Assurance engagements;

Technical, Professional and Ethical Standards?

(vi) Provisions of the relevant statutes and / or rules or regulations which are applicable in the context of the specific engagements being reviewed including instructions, guidelines, notifications, directions issued by regulatory bodies as covered in the scope of assurance engagements.

Professional & Technical Standards



Review of internal policies of PU

- Does the Practice Unit have an established plan for personnel needs at all levels, based on current and anticipated clientele, business growth, impending retirements, etc.
- Does the Practice Unit have an established recruitment policy.
- Are applicants and new personnel informed of the personnel policies and procedures relevant to them.
- Does the practice unit have continuing education programmes for partners and staff.
- How easily the current and relevant professional literature, including Accounting and Auditing Standards and pronouncements by professional bodies are available to the partners and staff.
- Does the practice unit conduct programmes for developing expertise in specialised areas and industries.

Compliance with professional & technical standards

PU to remain independent all the times

- PU set up policies and procedures to ensure that the PU and its partners and professionals are and remain independent at all times? - Annual declaration from all the partners.

- How did the PU communicate its independence requirements to its clients – Process of verifying independence in all fresh engagements

- Cases of withdrawal of engagement

Compliance procedures – Technical Standards

- Obtain the years of professional experience in practice
- Understand the field of expertise of such PU
- Whether the PU complies with the Accounting Standards issued by ICAI while performing the audit of its clients
- Whether the Secretarial Standards issued by Institute of Company Secretaries of India have been complied with wherever necessary
- Whether Framework for the preparation and presentation of Financial Statements are followed by the PU
- Whether going concern assumptions have been appropriately considered by the PU

Compliance procedures – Technical Standards

- Whether Standards on Auditing, Standards on Assurance Engagements, Standards on Quality Control and Guidance Notes on related services have been complied with by the PU
- Whether the relevant notifications/directions issued by ICAI have been considered by the PU
- Whether the samples collected by the PU are sufficient and appropriate to draw conclusions or provide an opinion
- Whether material facts are appropriately being disclosed by PU in case of any Audit clients
- Whether working papers are properly maintained by the PU and process

Key Checks - SA's

SA 210 Agreeing the Terms of Audit Engagements: -

•Check whether the scope and roles and responsibilities have been clearly brought out.

•The reviewer should verify whether the fees quoted in engagement letter is reasonable.

SA 220 Quality Control for an Audit of Financial Statements: -

•The reviewer should assess at the firm level and at the engagement level, the quality control as required by this Standard.

•The reviewer should access the leadership responsibilities for quality on audits, whether the practice unit follows relevant ethical requirements, whether the practice unit follows acceptance and continuance of client relationships.

•The reviewer should also access whether the engagement performance is being monitored.

Key Checks - SA's

SA 240 The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements: -

- The reviewer should verify whether the auditor has inquired the management, internal audit team and those charged with governance of any instance of actual or alleged fraud that has occurred in the past and obtain their respective views on the risk of fraud.

- The reviewer should verify whether the auditor has identified any unusual or unexpected relationship while performing analytical procedure and whether he has evaluated them to assess the risk of material misstatement due to fraud.

- The reviewer should verify whether the auditor has investigated any inconsistent responses from the management related to the inquiries.

Key Checks - SA's

Revised SA 260 Communication with Those Charged with Governance: -

•The reviewer should verify whether significant findings from the audit have been communicated to those charged with governance.

•The reviewer should verify whether the form, timing and expected general content of communications have been communicated to those charged with governance.

Key Checks - SA's

SA 300 Planning an Audit of Financial Statements: -

The reviewer needs to verify whether the auditor has documented –

- overall audit strategy
- audit plans
- significant changes made during the audit engagement to the overall audit strategy or the audit plan, and the reasons for such changes.

SA 320 Materiality in Planning and Performing an Audit: -

- The reviewer shall verify whether the auditor has determined Materiality and Performance Materiality when planning an audit.
- The reviewer shall verify whether the auditor has documented the following-
- Materiality for the financial statements as a whole
- If applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures
- Performance materiality

Key Checks - SA’s

SA 330: The Auditor’s Responses to Assessed Risks: -

•The reviewer shall verify whether the auditor has documented the following-

•overall responses to address the assessed risks of material misstatement at the financial statement level, and the nature, timing and extent of the further audit procedures performed;

•linkage of those procedures with the assessed risks at the assertion level;

•results of the audit procedures, including the conclusions where these are not otherwise clear.

SA 530 Audit Sampling: -

•The reviewer should verify whether the auditor has considered the purpose of the audit procedure and the characteristics of the population when designing an audit sample.

- The reviewer should identify whether the sample size selected by the auditor is sufficient to reduce sampling risk to an acceptably low level.
- The reviewer should verify whether the auditor has selected items for the sample in such a way that each sampling unit in the population has a chance of selection.

Accounting Standards / IND AS

1. AS 1 Disclosure of Accounting Policies
2. AS 2 Valuation of Inventories
3. AS 9 Revenue Recognition
4. AS 10 Property, Plant and Equipment
5. AS 11 The Effects of Changes in Foreign Exchange Rates
6. AS 15 Employee Benefits
7. AS 16 Borrowing Cost
8. AS 18 Related Party Disclosures
9. AS 22 Accounting for Taxes on Income
10. AS 29 Provisions, Contingent Liabilities and Contingent Asset

Commonly found Errors in Disclosure Requirements

XYZ Private Limited
`Balance Sheet as at Mar 31, 20xx

Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
4) Current liabilities (a) Short-term borrowings (b) Trade payables (c) Other current liabilities (d) Short-term provisions			

`Balar

Correct Disclosure

Refer Notification dated 4th september, 2015.

(b) Trade payables:-

(A) total outstanding dues of micro enterprises and small enterprises; and

(B) total outstanding dues of creditors other than micro enterprises and small enterprises.]

This is a wrong disclosure

Particulars		Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
4) Curre (a) Short-term bo (b) Trade payables (c) Other current liabilities (d) Short-term provisions			

XYZ Private Limited
Balance Sheet as at Mar 31, 20xx

Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
II. ASSETS Non-current assets (1) (a)Fixed Assets (i) Tangible assets (ii) Intangible assets (iii) Capital work-in-progress (iv) Intangible assets under development			

XYZ Private Limited
Balance Sheet as at Mar 31, 20xx

Correct Disclosure

Refer Notification dated 11th October 2018.

(1) (a) Property, Plant and Equipment and Intangible assets

Substituted by Amendment to Schedule III to the Companies Act, 2013. Effective from 01st April 2021

(i) Property, Plant and Equipment

Particulars			end of the previous
II. ASSETS Non-current assets (1) (a)Fixed Assets (i) Tangible assets (ii) Intangible assets (iii) Capital work-in-progress (iv) Intangible assets under development			

XYZ Private Limited
Balance Sheet as at Mar 31, 20xx

Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
(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			

XYZ Private Limited
Balance Sheet as at Mar 31, 20xx

Particulars
(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

Q. **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).
(ii) Earmarked balances with banks (for example, for unpaid dividend) shall be separately stated.
(iii) Balances with banks to the extent held as margin money or security against the borrowings, guarantees, other commitments shall be disclosed separately.
(iv) Repatriation restrictions, if any, in respect of cash and bank balances shall be separately stated.
(v) Bank deposits with more than twelve months maturity shall be disclosed separately.

Cash & Cash equivalents

(Refer Para 6.3 & 6.4 of ICAI GN on the Schedule III to the Companies Act, 2013)

- According to AS-3 Cash Flow Statements, Cash is defined to include cash on hand and demand deposits with banks. Cash Equivalents are defined as short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.
- Normally, deposits with original maturity of three months or less only should be classified as cash equivalents.
- Further, bank balances held as margin money or security against borrowings are neither in the nature of demand deposits, nor readily available for use by the company, and accordingly, do not meet the aforesaid definition of cash equivalents.
- Apparent conflict between the requirements of the Schedule III and the Accounting Standards

Cash & Cash equivalents

(Refer Para 6.3 & 6.4 of ICAI GN on the Schedule III to the Companies Act, 2013)

- As laid down in the General Instructions, Para 1 of Schedule III, requirements of the Accounting Standards would prevail over the Schedule III and the company should make necessary modifications in the Financial Statements, which may include addition, amendment, substitution or deletion in the head/sub-head or any other changes interse.
- The conflict should be resolved by changing the caption "Cash and cash equivalents" to "Cash and bank balances," which may have two sub-headings, viz., "Cash and cash equivalents" and "Other bank balances."
- The former should include only the items that constitute Cash and cash equivalents defined in accordance with AS 3 (and not the Schedule III)
- The remaining line-items may be included under the latter heading.

Other Bank Balances

- balances with banks to the extent held as margin money or
- security against borrowings etc
- bank deposits with more than three months maturity
- Banks deposits with more than twelve months maturity will also need to be separately disclosed

The non-current portion of each of the above balances will have to be classified under the head "Other Non-current assets" with separate disclosure thereof.

Commonly found Errors in CARO Reporting

CARO - Applicability

The Order provides that it shall not apply to:

a banking company, an insurance company, a section 8 company, a One person Company and a Small Company as defined under clause (85) of the section 2 of the Act;

(v) a private limited company, not being a subsidiary or holding company of a public company, having a paid up capital and reserves and surplus not more than rupees one crore as on the balance sheet date and which does not have total borrowings exceeding rupees one crore from any bank or financial institution at any point of time during the financial year and which does not have a total revenue as disclosed in Schedule III to the Act, (including revenue from discontinuing operations) exceeding rupees ten crores during the financial year as per the financial statements.

CARO- Paragraph 3(i)(a)(A)

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 (emphasis supplied).

CARO- Paragraph 3(i)(a)(A)

It was observed that in the first case, the auditor has reported that the company has maintained reasonable records. It was viewed that such reporting does not clearly indicate whether proper records are being maintained or not.

In the second case, the usage of the word 'generally' by the auditor gives an impression that there might exist certain instances where proper records of fixed assets have not been maintained.

the stated reports are ambiguous and cannot be considered to be strictly in line with the requirements of the said clause.

CARO- Paragraph 3(i)(b)

Fixed assets have been physically verified by the management and no material discrepancies were noticed on such verification

CARO- Paragraph 3(i)(b)

The Order requires the auditor to report whether the management has verified the fixed assets at reasonable intervals.

While an annual verification may be reasonable, it may be impracticable to carry out the same in some cases.

Even in such cases, the verification programme should be such that all assets are verified at least once in every three years.

Where verification of all assets is not made during the year, it will be necessary for the auditor to report that fact, but if he is satisfied regarding the frequency of verification he should also make a suitable comment to that effect.

➢ Statutory Dues [Paragraph 3(vii)(a)]

Whether the company is <u>regular</u> in depositing undisputed statutory dues including Provident Fund, employees' State Insurance, Income-tax, Sales-tax, Service Tax, duty of customs, duty of excise, value added tax, cess and any other statutory dues to the appropriate authorities and

if not, the extent of the arrears of outstanding statutory dues as on the last day of the financial year concerned for a period of more than six months from the date they became payable, shall be indicated

Disputed vs Undisputed - Need positive evidence or action on the part of the company to show that it has not accepted the demand for payment of tax or duty

CARO

Statutory Dues

- **“Dues” include taxes, interest & penalty**

a) Regular Payment

b) Generally Regular but slight delay in a few months

c) Not regular but delay not serious

d) Not regular and serious delay

As per ICAI GN on CARO, the above four situations warrants different disclosure.

The concept of Materialty to be kept in mind

CARO

Statutory Dues

1. Regular Payments throught the year

➢ **“undisputed statutory dues including……. and GST have been regularly deposited by the company with the appropriate authorities in all cases during the year”.**

2. Generally Regular but slight delay in a few months

➢ **“undisputed statutory dues including……. and GST have been regularly deposited by the company with the appropriate authorities though there has been a slight delay in a few cases”.**

CARO

Statutory Dues

3. Not Regular but delay not serious

- **“undisputed statutory dues including……. and GST have not generally been regularly deposited with the appropriate authorities though the delay in deposit have not been serious.**

4. Not Regular and serious delay

- **“undisputed statutory dues including……. and GST have not been regularly deposited with the appropriate authorities though there have been serious delays in a large number of cases”.**

Non - Compliance of Accounting Standard

AS 1 - Disclosure of Accounting Policies

FRRB Observations on Accounting Standards AS-1

1. From the notes to accounts given In the Annual Report of a company, it has been noted that accounting policies were given under various notes to accounts instead of stating all such policies under a single head of significant accounting policies.

Non compliance with para 25 of AS 1 – Disclosure of Accounting Policies. The said para requires that 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 in one place.

2. Contingent liabilities has been disclosed under various notes instead of disclosing the same at one place

Paragraph 20 of Accounting Standard (AS) 1, 'Disclosure of Accounting Policies', states:

"It would be helpful to the reader of financial statements if they are all disclosed as such in one place instead of being scattered over several statements, schedules and notes."

Hence, it was viewed that the presentation of the information has not been made as required by the spirit of paragraph 20 of AS 1

FRRB Observations on Accounting Standards AS-1

1. Impairment losses, if any, are recognised in accordance with the accounting standard issued in this regard by the Institute of Chartered Accountants of India.
2. Provision for Current Tax been made as per the provisions of Income Tax Act, 1961 and adjustment for Deferred Tax is made in accordance with Accounting Standard-22

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. (Para 11 of AS 1)

Companies have merely mentioned in their accounting policies that they are in accordance with the requirements of the accounting standards as issued by the Institute.

It was viewed by FRRB that the accounting policies should be explicitly stated.

Reference should have been made to the Accounting Standards notified under the Companies (Accounting Standards) Rules 2006, rather than those issued by the Institute of Chartered Accountants of India.

FRRB Observations on Accounting Standards AS-1

1. Income is recognised on accrual basis.
2. Sales comprises sale of goods net of excise duty and include export benefits.
3. Revenue is recognised and expenditure is accounted for on their accrual.

The policies above omit to state explicitly the point of time when significant risks and rewards in goods stand transferred to the buyer and revenue is recognised in the books of accounts.

The policy regarding timing of recognition of revenue arising from sale is an important accounting policy for any company and therefore, it should be disclosed as per the requirements of paragraph 24 of AS 1.

FRRB Observations on Accounting Standards AS-1

In one of the Annual Report the accounting policy is stated as follows:

“The unrealised loss on outstanding derivative contracts had not been recognised in the books, considering the principles of prudence as enunciated in AS 1. “

It was viewed that as per paragraph 17 of AS 1 prudence norms prohibit recognition of future expected profits but not the recognition of future expected losses. Accordingly, in the stated policy the prudence principles of AS 1 has not been correctly interpreted.

FRRB Observations on Accounting Standards AS-1

Subsidies granted by the government for providing telecom services in rural areas are recognized as other operating income in accordance with the relevant terms and conditions of the scheme and arrangements.

The timing of recognition of such grant is not clear from the stated policy. Such policy only provides a means to understand the accounting policy adopted for recognition of government grant, rather than explicitly disclosing the principles adopted for the same. Accordingly, it was viewed that the requirements of AS 1 has not been complied with.

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Non - Compliance of Accounting Standard

AS 2 - Inventories

FRRB Observations on Accounting Standards – AS 2

1. Useful designs are valued at actual cost and Stock in progress is valued at direct cost
2. Bunkers remaining on Board are valued at weighted average cost.
3. Raw materials and stores and spares are valued at cost.
4. Raw Material & Components, Stores and Spares, Die Steel Blocks are valued at cost and Work in progress is valued at estimated cost.

In the above cases, the inventories have been stated to be valued only at cost. paragraph 5 of AS 2 requires that inventories should be valued at the lower of cost and the net realisable value.

Accordingly, the stated accounting policies are not in line with the requirements of AS 2.

Further, the cost formula used for valuation of inventories, is required to be disclosed as per paragraph 26(a) of AS 2.

FRRB Observations on Accounting Standards – AS 2

- **The schedule of 'Inventories' given in the Annual Reports of some companies, inventories were described "as taken, valued and certified by the management."**

ICAI Guidance Note on Audit of Inventories, has clarified that the use of expression 'as valued and certified by the management' may lead the users of financial statements to believe that the auditor merely relies on the management's certificate without carrying out any other appropriate audit procedures to satisfy himself about the existence and valuation of inventories.

Therefore, usage of phrase viz "as valued and certified by the management" indicates that there is a disclaimer for inventories which should be avoided.

ICAI GN further states that auditors may advise their clients to omit the expression "as valued and certified by the management", when describing inventories in the financial statements.

FRRB Observations on Accounting Standards – AS 2

- **Inventories are valued at cost or net realisable value, whichever is lower. Costs comprise all cost of purchase, cost of conversion and other costs incurred in bringing the inventories to their present location and condition. ‘First-in- first-out’ or ‘Average cost’ method is followed for determination of cost.**

As per Para *16 - The cost of inventories, other than those dealt with in paragraph 14, should be assigned by using the first-in, first-out (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 condition.*

The company has used the ‘Average Cost’ method and not the ‘weighted average cost’ method for the determination of cost, which is not in line with the requirement of paragraph 16 of AS 2.

FRRB Observations on Accounting Standards – AS 2

➢ From the schedule of Current Assets given in the Annual Report of a company, it has been noted that Stock in Trade also includes the stock of DEPB Receivables as well as Plant & Machinery retired from active use.

As per para 3.1 Inventories are assets:

held for sale in the ordinary course of business;

in the process of production for such sale; or

in the form of materials or supplies to be consumed in the production process or in the rendering of services."

DEPB Receivables should be treated as a part of loans and advances and it should not be included in stock in trade.

Further, the Plant & Machinery retired from active use is a part of fixed assets; hence, it should also be not included in stock in trade. It was viewed that such assets should have been shown separately in the fixed assets schedule as "held for disposal".

Non - Compliance of Accounting Standard

AS – 3 Cash Flow Statements

FRRB Observations on Accounting Standards – AS 3

In the Cash Flow Statement of a non financial enterprise, under the heading of financing activities, an item interest (net) amounting to Rs. XXX has been reported.

Paragraph 30 of AS 3

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 can not be netted off against each other.

FRRB Observations on Accounting Standards – AS 3

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

Paragraph 34 & 35 of AS 3

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'.

FRRB Observations on Accounting Standards – AS 3

In one of the enterprise, 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, Interest accrued on Fixed Deposits and the total of these components matches with the closing cash & cash equivalents as reported in the cash flow statement.

Paragraph 5.2 of AS 3

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, accrued interest on FDs 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

FRRB Observations on Accounting Standards – AS 3

In certain enterprises, the Cash & Cash equivalent as reported in the Notes and Cash Flow Statement does not tally and reconciliation was not given.

Paragraph 42 of AS 3

There is a mismatch between the amounts of Cash & Cash Equivalent reported at two places in the same set of financial statements. It was viewed that since the balances do not tally with each other, therefore, the reconciliation should have been provided for better understanding of the reader of the financial statements

FRRB Observations on Accounting Standards – AS 3

From the Cash Flow Statement given in the Annual Report of a company it was noted that 'fixed assets lost due to robbery' were disclosed under the head 'Cash Flow from Investing Activities.'

Paragraph 40 of AS 3

It was viewed that loss of fixed assets due to theft/ robbery is a non cash transaction hence, it should have been excluded from Cash Flow Statement as per the above-stated requirement.

It was further noted that loss on fixed assets lost in robbery has already been adjusted to determine 'cash flow from operations'. Hence, showing separate cash outflow for same loss which is a non-cash transaction is unwarranted.

Non - Compliance of Accounting Standard

AS 4 - Contingencies and Events Occurring After the Balance Sheet Date

FRRB Observations on Accounting Standards – AS 4

One of the Notes to Accounts states that it is the Company's Policy to take into account the impact of any significant event that occurs after Balance Sheet date but before the *finalisation of accounts (emphasis supplied)*.

Paragraph 3.2 of AS 4

It was viewed that events occurring after the balance sheet date are those significant events that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors/ corresponding approved authority. It was viewed that the date of finalisation of accounts could not be construed as the date when the financial statements have been approved by the Board unless the date of signing the Auditors' Report is same as the date of finalisation of accounts.

Non - Compliance of Accounting Standard

AS 7 - Construction Contracts

FRRB Observations on Accounting Standards – AS 7

The significant accounting policy relating to construction contracts states as below:

"Job work revenue is accounted on the basis of running bills raised and approved by the clients. Revenue Expenditure is accounted on accrual basis as and when it is incurred."

Paragraph 21 of AS 7

It was observed that revenue has been recognised based on bills raised and cost has been accounted, as and when incurred, whereas paragraph 21 of AS 7 requires to recognise revenue and costs based on the stage of completion of the contract activity as on the reporting date. Thus, the policy regarding construction contracts is not in line with the requirement of AS 7, Construction Contracts.

FRRB Observations on Accounting Standards – AS 7

From the Annual Report of a company, it was noted that the company is involved in construction business and its Schedule of inventory also include an item of Job in progress. However, no other disclosure was made in the financial statements.

Paragraph 39 of AS 7

It was observed that though involved in construction business, company had not made the following disclosures, as is required by Paragraph 39 of AS 7:

the aggregate amount of costs incurred and recognised profits (less recognised loses) up to the reporting date;

the amount of advances received ; and

the amount of retentions.

Accordingly, it was viewed that the company has not complied with the requirement of AS 7.

Non - Compliance of Accounting Standard

AS 9 - Revenue Recognition

FRRB Observations on Accounting Standards – AS 9

- **Sales revenue is recognised when property in the goods with all significant risk and rewards as well as the effective control goods usually associated with ownership, are transferred to the buyer, at a price and includes excise duty and exchange fluctuation in case of the export.**

As per 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, from the rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends...”

The foreign exchange fluctuation is not an inflow of cash receivable etc. arising from the sale of goods but from settlement of non- monetary item. Hence, accounting such fluctuation as part of Sales revenue is not in accordance with the aforesaid paragraph of AS 9.

FRRB Observations on Accounting Standards – AS 9

- **Sales include duty drawback, license premium on exports, and insurance claims on stocks and are recorded net of trade discounts and other rebates.**

As per 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, from the rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends. Revenue is measured by the charges made to customers or clients for goods supplied and services rendered to them and by charges and rewards arising from the use of resources by them…..

Duty drawback, license premium on exports and insurance claims on stocks/ have not been disclosed separately, instead the reported sales have been increased by them.

The receipts from said items is not a consideration arising from sale of goods. Hence, they should not be merged with the sales and should be disclosed as separate line items. This aspect has also been explained in the Expert Advisory Opinion (Query No. 1.15, Volume VI, page 43).

FRRB Observations on Accounting Standards – AS9

➢ **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.**

It may be noted that the ICAI has issued an Announcement titled as 'Treatment of Inter-divisional Transfers', which provides that:

"Since in case of inter- divisional transfers, risks and rewards remain within the enterprise and also there is no consideration from the point of view of the enterprise as a whole, the recognition criteria for revenue recognition are also not fulfilled in respect of inter-divisional transfers."

Thus, the recognition of inter- divisional transfers as sales indicates an inappropriate recognition of revenue, which is not in line with AS 9.

FRRB Observations on Accounting Standards – AS9

From the Annual Reports of some companies, it has been noted that one of the items of income as shown in the Statement of Profit and Loss is income from advertisement and ticket sales and the related accounting policy states as follows:

'Revenue from sale of tickets is recognised when the tickets have been sold. Advertisement revenue is recognised when advertisements and net realisation are confirmed.'

- Para 12 of AS 9
- It was noted that the enterprise under review render services. Therefore, revenue from sale of tickets should be recognised as per the completed contract method.
- Same principle is applicable to income from advertisement as well

FRRB Observations on Accounting Standards – AS9

From the Annual Report of a company, it has been noted that the company has recognised 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 realisable value and insurance claim against the same is taken as other income. Insurance claim against loss of fixed assets has also been recognised based on the claim filed with the insurance company. The note further states that said income has been recognised as per the AS 9

Para 4.1 & 9.2 of AS 9

FRRB Observations on Accounting Standards – AS9

Para 4.1 & 9.2 of AS 9

It was noted that insurance claims do not fall within the definition of 'Revenue' as given in AS 9.

Insurance claims also requires that the amount realisable is measurable and it is not unreasonable to expect ultimate collection

Recognising insurance claims at the time of filing the claims with the insurance company without considering the uncertainty relating to its measurability is not appropriate.

Accordingly, it was viewed that recognition of revenue at the time of filing of claims is not in line with the principles of AS 9.

FRRB Observations on Accounting Standards – AS9

The accounting policies regarding recognition of dividend income has been disclosed as follows in the Annual Reports of some companies:

Dividend is accounted as and when received.

Income & Expenditures are recognised on accrual basis except dividend on shares and units of Mutual Funds, which are recognised on cash basis

- **Para 13 of AS 9**

It was observed that the dividend income has been recognised on receipt basis while paragraph 13 of AS 9 requires recognition of dividend income when the right to receive payment is established.

Accordingly, it was viewed that the recognition of dividend income on receipt basis is not in line with the requirements of AS 9.

Non - Compliance of Accounting Standard

AS 10 – Property, Plant & Equipment

Accounting Standards – AS10

➢ ***Property, plant and equipment are stated at cost of acquisition or construction less accumulated depreciation less accumulated impairment, if any.***

Elements of Cost

Para 17. The cost of an item of property, plant and equipment comprises:

(a) its purchase price, including import duties and non –refundable purchase taxes, after deducting trade discounts and rebates.

(b) any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

Non - Compliance of Accounting Standard

AS 11 - The Effects of Changes in Foreign Exchange Rates

FRRB Observations on Accounting Standards – AS 11

- In the accounting policy of foreign exchange, it was stated that if foreign exchange transactions relates to acquisition of fixed assets, they are adjusted to the carrying cost of such assets

- **Paragraph 46A of AS 11**

It was noted from the stated accounting policy that the foreign exchange differences related to acquisition of any fixed asset are adjusted to the cost of such assets. It was viewed that such adjustment is permitted only if such exchange difference has arisen on long term foreign currency monetary items incurred for acquisition of a depreciable fixed asset.

It was noted that in the given case neither the stated accounting policy nor the Balance Sheet indicates existence of any long term foreign currency monetary item. Hence, adjustment of any foreign exchange rate variation to the cost of fixed asset was not in line with the requirements of AS 11.

FRRB Observations on Accounting Standards – AS 11

From the accounting policy given in the Annual Report of a Company, it was noted that the export sales have been recorded at the rate notified by the customs for invoice purposes.

- **Paragraph 9 of AS 11**

It was noted from the stated accounting policy that the export sales have been recorded at the rate notified by the customs for invoice purposes instead of translating the same on the basis of exchange rate prevailing on the date of transaction. This is not in line with the principles enunciated in paragraph 9 of AS 11.

Non - Compliance of Accounting Standard

AS - 15 Employee Benefit

FRRB Observations on Accounting Standards – AS 15

- Provision for gratuity has been made on the basis of actuarial valuation in the accounts in respect of employees who have completed qualifying period of service.

Question No. 14 of ASB Guidance on Implementing AS 15, Employee Benefits (revised 2005), issued by the Accounting Standards Board, states as follows:

"In this case, 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. 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

Keeping in view of the above, it was felt that the provision should be created in respect of gratuity payable during the first five years of service for all employees rather than creating provision for those employees who have completed qualifying period of service.

FRRB Observations on Accounting Standards – AS 15

- **The accounting policy on gratuity states that "Provision for gratuity is made in the accounts, considering the Balance sheet date as the notional date of retirement".**

Paragraph 68 of AS 15

It has been noted that as per AS 15 the provision for gratuity should be determined through actuarial valuation which should be based on assumption that are not excessively conservative and should reflect the economic relationship considering the factors. It was viewed that the policy adopted by the company indicates that while making provision, it is assumed that each of its employee retire on the balance sheet date which is an excessively conservative assumption and also does not reflect the economic relationship between factors such as inflation, salary increase, the return on plan and discount rates. Since it does not consider actuarial risk while valuing its liability towards gratuity, it was viewed that actuarial valuation is not followed by the company. It is against the requirements of AS 15

FRRB Observations on Accounting Standards – AS 15

From the financial statements of certain companies it has been noted that they do not provide the accounting policy on employee benefits (including defined benefit plans) and in many of the cases reviewed by the FRRB, the disclosures required under Paragraph 120 were not given or partially given by the enterprises

Paragraph 119 and 120 of AS 15

In majority of the cases it was observed that enterprises have not disclosed the basic information about the defined benefit plan as required under paragraph 119. Further, the description of defined benefit plan and accounting policy adopted for actuarial gains and losses including various other disclosures of paragraph 120 are, *inter alia*, the commonly found mistakes in the financial statements of enterprises.

Non - Compliance of Accounting Standard

AS 16 – Borrowing Cost

FRRB Observations on Accounting Standards – AS 16

Accounting policy on Valuation of Inventories states that – Finished goods are valued at lower of cost or net realisable value; cost includes depreciation, *interest* (excluding interest on discounting of bills) and direct expenses to the point of stocking, excise duty but excludes administration and selling expenses.

AS 2 and AS 16

It was noted that interest cost was included in the cost of inventories. **Para 12 of AS 2**,'Valuation of Inventories' provides that interest and other borrowing costs are usually considered as not relating to bringing the inventories to their present location and condition and are, therefore, usually not included in the cost of inventories.

Para 5 of AS 16, 'Borrowing Costs' provides that those inventories that are routinely manufactured or otherwise produced in large quantities on a repetitive basis over a short period of time, are not qualifying assets.

Accordingly**, it was viewed that as per AS 16, no borrowing cost (interest) can be capitalised unless such inventories take a substantial period of time to get ready for sale**. Thus there is a non compliance of AS 2 as well as AS 16.

FRRB Observations on Accounting Standards – AS 16

Schedule of secured loans as well as related information as given in notes to accounts of a Company, reflects that certain borrowing cost has been incurred during the year, a portion of which has been capitalised to the value of fixed assets and rest of portion has been expensed.

Paragraph 23 of AS 16

It may be noted that Paragraph 23 of AS 16, requires that the financial statements should disclose:

a) the accounting policy adopted for borrowing costs; and

b) the amount of borrowing costs capitalised during the period."

It was observed **that although the company had capitalized a signification portion of financial charges to the value of fixed assets but omitted to disclose the accounting policy as adopted by it for borrowing cost**.

It is not in line with the requirement of paragraph 23 of AS 16.

Non - Compliance of Accounting Standard

AS 22 - Accounting for Taxes on Income

FRRB Observations on Accounting Standards – AS 22

Is it necessary to disclose the break-up of the Deferred Tax Liability/ Deferred Tax Asset either in the schedule or notes to accounts.

Para 31 of AS 22

Para 31 of AS 22, Accounting for Taxes on Income, requires that " the break-up of deferred tax assets and deferred tax liabilities into major components of the respective balances **should** be disclosed in the notes to accounts."

Non disclosure of break-up of deferred tax assets or deferred tax liability is in contravention of AS 22.

FRRB Observations on Accounting Standards – AS 22

The accounting policy relating to deferred tax states that "Deferred tax liability and asset are recognised, subject to the consideration of prudence, on timing differences using the tax rates substantively enacted on the Balance Sheet date."

Para 15 of AS 22

It has been noted from paragraph 15 of AS 22 that **deferred tax assets should be recognised and carried forward only to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realised.**

It has been noted that although the deferred tax asset has been recognised, however, it is not clear as to whether there exists reasonable certainty that sufficient future taxable income would be available against which such deferred tax assets could be realised.

Thus, the stated accounting policy with regard to recognition of Deferred Tax Assets is not complete.

FRRB Observations on Accounting Standards – AS 22

The deferred tax assets and liabilities had been presented in either of the manner as given below:

- Deferred tax liability shown as a part of ‘Loan Funds’.
- Deferred tax (net) shown after the head ‘Net Current Assets’.
- Deferred tax Liability is shown as a deduction from the ‘Application of Funds’.
- Deferred tax Liability is shown as a part of ‘Shareholders Funds’.
- Deferred tax Liabilities is shown as distinct sub-head under the Schedule of Provisions.

Paragraph 30 of AS 22

Explanation to Paragraph 30 of AS 22 requires that **deferred tax liabilities should be disclosed on the face of the balance sheet separately after the head ‘Unsecured Loans’ and deferred tax assets should be disclosed on the face of the balance sheet separately after the head ‘Investments’.**

Accordingly, it was viewed that the aforesaid presentation of DTA/ DTL is not in line with AS 22.

Non - Compliance of Accounting Standard

AS 29 - Provisions, Contingent Liabilities and Contingent Assets

FRRB Observations on Accounting Standards – AS 29

- **From the Annual Report of a company, it has been noted from accounting policy on Revenue Recognition that no provision has been made for possible returns or expenses during the warranty period**

- **It may be noted that the definition of the term 'provision' as defined in paragraphs 10.1 and 10.2 of AS 29, provides as follows:**

***"10.1 A provision** is a liability which can be measured only by using a substantial degree of estimation."*

***10.2 A liability** is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits."*

It was noted that obligation in respect of sales return can be estimated reliably on the basis of past experience and other relevant factors and a provision in respect of sales returns should be recognised; otherwise, the company should postpone the recognition of revenue on such sales.

In light of above, it was viewed that the requirements of either AS 29 or AS 9 have not been complied with.

FRRB Observations on Accounting Standards – AS 29

- From the Annual Report of company, it has been noted that from notes relating to Long-term Provisions and Short-term Provisions that “Provision for Expenses” has been included under these heads

It was noted that provisions are made for those liabilities, the measurement of which involves substantial degree of estimation and which will be settled in future.

Expenses are generally considered as accrued against services that have been received but not settled.

Therefore, it was viewed that the disclosure of unpaid expenses under the head of provisions is not in accordance with paragraph 12 of AS 29.

Key Checks - Accounting Standards

AS-9/Ind AS 18 - Revenue Recognition: -

•Have you ensured that revenue is recognized only when there is certainty to its collection.

•Have you ensured the following in case of performance in rendering of services:

- Method of recognizing revenue is either completed service contract method or proportionate completion method.
- There is no significant uncertainty regarding amount of consideration.

•Check whether a provision has been made to reflect the uncertainty where uncertainty relating to collectability arises subsequent to recognition.

Key Checks - Accounting Standards

AS-17/Ind AS 108 - Segment Reporting: -

- Whether primary and secondary segment reporting formats been identified correctly
- Whether the segment revenue includes only that portion of enterprise revenue which is directly attributable to a segment or portion of revenue attributable to particular segment or revenue from transactions with other Segments
- Whether identification of amounts with particular segment is appropriately made to measure the segment revenue, segment expense, segment assets and liabilities of reportable segments is done
- Whether proper disclosures of primary and secondary activities have been considered by the PU

Key Checks - Accounting Standards

AS-18/Ind As 24 - Related Party Disclosures: -

•Whether the PU has obtained the list of related party details which is signed by the client

•Has the PU co related the transaction recorded in the register maintained u/s 189 of Companies Act, 2013

•Whether the disclosure requirement under this Standard has been considered by the PU

AS-21/Ind As 110 - Consolidated Financial Statements: -

•Has the PU obtained the list of associate/subsidiary/joint venture from the client

•Whether the PU has considered the consolidated financial statements in case the client has either an associate/subsidiary/joint venture

•Whether the reasons for not consolidating either an associate/subsidiary/joint venture been disclosed in the consolidated financial statements

Key Checks - Ind AS

AS 10/Ind AS 16- "Property, Plant and Equipment“: -

•The reviewer needs to identify whether the PPE has appropriately been measured by the business unit as per Ind AS 16.

•The reviewer needs to identify whether appropriate disclosures have been made by the business unit for PPE as per Ind AS 16 including-

- measurement bases used
- depreciation method used
- useful life or the depreciation rates used
- the gross carrying amount and the accumulated depreciation at the beginning and end of the period
- the existence and amounts of restrictions on title and PPE pledged as security for liabilities
- impairment losses recognized/reversed in profit or loss in accordance with Ind AS 36
- assets classified as held for sale in accordance with Ind AS 105.

Key Checks - Ind AS

AS 24/Ind AS 38-"Intangible Assets“: -

•The reviewer needs to identify whether the intangible assets have appropriately been measured by the business unit as per Ind AS 38.

•The reviewer should identify whether the business unit has disclosed the following for each class of intangible assets, distinguishing between Internally generated intangible assets and other intangible assets-

- whether the useful lives are indefinite or finite and if finite the useful lives or amortization rates used
- the gross carrying amount and the accumulated amortization at the beginning and end of the period
- impairment losses recognized/reversed in profit or loss in accordance with Ind AS 36
- increases or decreases during the period resulting from revaluations or impairment
- The reviewer should also identify the aggregate amount of research and development expenditure recognized as an expense during the period

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