



# Schedule VI and statutory reporting formats vis-à-vis accounting standards

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# Format of financial statements and accounting standards

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- Prescribed under Schedule VI to the Companies Act, 1956
- Companies Bill 2008 does not intend to have a schedule
  - Will lay down format by way of rules
- IAS 1 provides general principles for presentation of financial statements
- UK Companies Act 2006 also lays down statutory format of financial statements
  - Pursuant to this, Large and Medium Sized Companies and Groups (Accounts and Reports) Regulations 2008 have been drawn up



# Revision of Schedule VI

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- In end-Nov 2008, the MCA initiated the process of revamping of schedule VI
- Objectives of the revamping exercise
  - Vast amount of change has taken place in business and industry since Schedule VI was laid down
  - Companies (Accounting Standards) Rules 2006 has been promulgated
  - Necessary to harmonise Schedule VI with accounting standards
  - At the same time, simpler reporting format for smaller companies
  - Removal of requirements of disclosures which have become redundant
- The Memorandum was put on the website of MCA for comments. Comment period expired on 22 Dec 2008



# Drafts of Revised formats

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- Two drafts of revised Schedule VI:
  - Main Schedule VI for Non-SMCs (Part C)
  - Saral Schedule VI for SMCs (Part D)
- SMCs defined the same way as under AS Rules
  - (i) whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;
  - (ii) which is not a bank, financial institution or an insurance company;
  - (iii) whose turnover (excluding other income) does not exceed rupees fifty crore in the immediately preceding reporting period;
  - (iv) which does not have borrowings (including public deposits) in excess of rupees ten crore at any time during the immediately preceding reporting period; and
  - (v) which is not a holding or subsidiary company of a company which is not a small and medium-sized company.
- This Schedule sets out the minimum requirements



# Key features

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- Classification of assets
  - based on liquidity
- Classification of expenses
  - Based on function, rather than nature



# Developments over Extant Schedule VI

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- removed statistical disclosure requirements as Part IV of Schedule VI.
- minimum disclosure requirements
- flexibility for amendments:
  - Schedule to automatically stand amended with reference to accounting standards
  - Disclosure requirements are in addition to accounting standards
- compatibility and convergence with IFRS
- Removal of distortions evaluating liquidity and solvency (i.e., current ratio)
- Rounding off made more logical and related to scale of operations
  - Millions are now statutorily included
  - Companies with turnover exceeding Rs 100 crores will report numbers in lakhs, millions, crores or decimals
- understandable, reliable, relevant and comparable financial reporting system



# Formats of financial statements

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- Same for SMCs and Non- SMCs
- Presentation based upon
  - Vertical format in case of B/S
  - Multi-step format in case of P/I
- Classification of assets and liabilities into
  - current and non-current
  - Terms defined as current asset & liability and operating cycle
- Key feature is liquidity-based classification of assets and liabilities
  - Current/non-current distinction is based on timing of cashflows
- The definition of current assets and current liabilities is almost the same as in IAS 1
  - The question is, why is Schedule VI needed at all?
  - Why not be content with an AS rather than schedule to the Act
  - Possibly due to the statutory requirements of the existing Act



# Statement of Profit & Loss

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- Key feature - while international reporting formats have a separate statement for OCI, Schedule VI misses that
  - Though we are switching over to fair value accounting soon
  - The idea of the mezzanine statement is to distinguish notional losses from real losses
  - We already have foreign exchange translation losses etc affecting revenues of most Indian companies
- Presentation based upon
  - Multiple step format
- Classification of expenses based upon:
  - Function of expense
    - For example, operating, financial, selling, administrative, development, etc
  - Most line items have to be classified based on their function
    - Even depreciation
      - Assets used for operations to be distinguished from other assets
- Different in case of SMCs



## Items on the balance sheet –liability side

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- Share capital
- Reserves and surpluses
- Long term borrowings
- Long term provisions
- Short term borrowings
- Short term provisions
- Trade payables
- Other current liabilities



# Items on the asset side

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- Tangible assets
- Intangible assets
- Non current investments
- Long term loans and advances
- Other non current assets
- Current investments
- Inventories
- Trade receivables
- Cash and cash equivalents
- Short-term loans and advances
- Other Current assets
- Contingencies and commitments
- Amount of dividends proposed to be distributed for the period, and amount per share; arrears of dividends on cumulative preference shares



# Additional disclosures in Balance sheet

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- The share capital details (authorised, issued, paid up) etc., have been shifted to notes to accounts
- Additional requirement
  - Shares in the company held by shareholders holding more than 5%
    - Apparently, list of shareholders holding more than 5% to be attached
  - Important disclosure about outstanding options:
    - shares reserved for issue under options and contracts/commitments for the sale of shares/disinvestment, including the terms and amounts



# Additional disclosures in balance sheet

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- Classification of loans into long-term and short term
  - In addition to secured and unsecured
- Additional disclosure in case of loans
  - Loans repayable on demand
  - Many loans/bonds might have an acceleration feature/puttable feature
    - Anything that, except in the event of a default, exposes a company to liquidity risk to be separately reported
- Period and amount of continuing default – distinguishing between interest and principal
  - Very significant, and surely, quite controversial point
  - This is applicable to both long term borrowings and short term borrowings
  - Most often, there are disputes as to defaults
    - Would be difficult for auditors to take a stand on whether a case of default
- Provisions classified into long-term and short term
  - The basis for long-term and short-term remains the same
    - based on 1 year liquidity



# Other significant points about balance sheet - investments

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- Notable point
  - Distinction between L&R, HTM assets, AFS assets and trading assets as required by AS 30 not observed here
- Investment property and land/buildings for self-use are distinguished
- In investments, one more item comes – investments in controlled special purpose entities
  - Commendable feature
  - Good to see that the MCA has learnt from on-going accounting developments in this regard (ED on special purpose entities issued by IASB, amendments already made by FASB)
- In case of trading entities, will investments be stock in trade:
  - Yes
  - As investment does not include stock in trade
    - Investment by definition is investment outside the business of the investing entity



## Disclosures in balance sheet

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- Earmarked cash and bank balances to be disclosed separately
- Bank deposits with more than 12 months' maturity separately shown
- Repatriation restrictions to be separately shown



# Statement of Profit & Loss

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- For non-SMCs, functional classification required
- For SMCs, classification based on nature of expense may suffice
  - IAS 1 provides entities with a choice to adopt function of expense method or nature of expense method



# Cash Flow Statement

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- Not in extant Schedule VI
- Now made a part of financial statements
- Cash inflow and outflow format
- Use of Indirect method
  - Deviation from IAS 7 & AS 3 which permit both direct and indirect methods



# Developments in P/L format

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- Done away with redundancies
  - capacity details
  - expenditure/income in foreign currency
  - details of debts/advances due from companies under same management (Better disclosure as per AS 18 on Related Party Disclosure)
  - quantitative information on inventories (covered under AS 17 on Segment Reporting)



	Particulars		Figures for the current reporting period		Figures for the previous reporting period
I.	Revenues from operations		XXXX		XXXX
II.	Cost of sales/services		XXXX		XXXX
III.	Gross profit (I – II)		XXXX		XXXX
IV	Operating expenses: (1) Selling and marketing expenses (2) Administrative expenses		XXXX XXXX		XXXX XXXX
	Total operating expense		XXXX		XXXX
V.	Results from operating activities (III – IV)		XXXX		XXXX
VI.	Non operating Income/expenses: (1) Gains/(Losses) on sale of long-term investments (2) Foreign currency exchange gains/(losses), net (3) Finance Cost (4) Other income (5) Other expenses		XXXX XXXX (XXXX) XXXX (XXXX)		XXXX XXXX (XXXX) XXXX (XXXX)
	Total Non Operating Income/expenses:		XXXX		XXXX
VII.	Income before income tax (V + VI)		XXXX		XXXX
VIII	Tax expense: (1) Current income tax (2) Deferred income tax (3) Others	XXXX XXXX XXXX		XXXX XXXX XXXX	
IX.	Profit for the period (VII – VIII)		XXXX		XXXX
X.	Earnings per equity share: (1) Basic (2) Diluted		XXXX XXXX		XXXX XXXX

Format of Profit and loss account



# Remarkable changes in P/L A/c

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- Accumulated loss as negative amount under reserves and surplus
- Allocation of operating expenses into selling and marketing expenses and administrative expenses:
  - All direct production overheads
  - Depreciation
  - Indirect overheads that can be allocated to production function
- Apportions common expenses to different functions/ activities
- Revised schedule uses term cost of sales instead of term cost of goods sold



# Functional classification – selling costs

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- (a) Payroll costs of sales, marketing and distribution functions (ESOP and ESPP expenses to be disclosed separately);
- (b) Advertising;
- (c) Sales persons' travel and entertaining;
- (d) Warehouse costs for finished goods;
- (e) Transport costs arising on the distribution of finished goods;
- (f) All costs of maintaining sales out-lets;
- (g) Agents commission payable;
- (h) Other selling and marketing expenses.



# SMCs (Saral Schedule VI)

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- Applies to SMCs defined in Rule 2(f) of Companies (Accounting Standards) Rules, 2006
- assumed that SMC's
  - No complex transactions
  - no public accountability
  - do not hold assets in a fiduciary capacity for a broad group of outsiders
  - accountability limited to owners and government authorities/agencies
- 'Users' and 'information needs' of the Users of financial statements of SMCs are limited



# Financial Statements formats

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- Balance Sheet format same as that of Non- SMCs
- Statement of P/L presentation based upon:
  - Single step format
  - Classification of expenses is based upon:
    - Nature of expense method



# Classification of Equity and Liability

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- Should classify redeemable preference shares as liability.
  - Though covered by AS 31 ( IAS 32).
- Does not cover disclosure requirements as regards puttable instruments classified as equity
  - covered by Para 136 A of IAS 1



# Further suggestions in revised format

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- Does not require separate disclosure of P/L items on account of exceptional events listed in IAS 1
  - a) write-downs of inventories to net realisable value or of property, plant and equipment to recoverable amount, as well as reversals of such write-downs;
  - (b) restructurings of the activities of an entity and reversals of any provisions for the costs of restructuring;
  - (c) disposals of items of property, plant and equipment;
  - (d) disposals of investments;
  - (e) discontinued operations;
  - (f) litigation settlements; and
  - (g) other reversals of provisions.
  
- Does not require separate disclosure of income from equity method associates and joint ventures
  
- Revised Balance format does not require separate presentation of Biological Assets



# Further suggestions in revised format

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- Formats for stand-alone financial statements
  - do not provide for consolidation related presentation like minority interest and parent's interest.
- minimum disclosures on the face of financial statements
- two-stage comprehensive income
- Notes or Schedules forming part of financial statements not sufficient



# Further points

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- No disclosure of accounting policies
  - This seems to be an inadvertent omission
- Sources of estimation uncertainty
  - Required to be separately disclosed as per IAS 1
- Objectives, policies and processes for managing capital required to be disclosed as per IAS 1
  - Capital is a significant cushion against risk of default
- Puttable financial instruments treated as equity



# IAS 1 and Schedule VI

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- The financial statements as IAS 1 are:
  - statement of financial position
  - statement of comprehensive income
    - Profit and loss account
    - Other comprehensive income
  - a statement of changes in equity
  - statement of cash flows
  - notes, comprising a summary of significant accounting policies and other explanatory information
  - In case of retrospective changes in accounting policy, statement of financial position at the beginning of such period
- Comparison with Schedule VI
  - The concept of OCI has been missed
  - OCI consists of fair value changes in response to accounting standards such as
    - changes in revaluation surplus
    - actuarial gains and losses on defined employee benefit plans
    - gains and losses arising from translating the financial statements of a
    - foreign operation
    - gains and losses on remeasuring available-for-sale financial assets
    - the effective portion of gains and losses on hedging instruments in a cash flow hedge (see IAS 39).



# Classification of current and non current assets

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- IAS 1 is also concerned with the classification of current/non-current assets
- Amounts expected to be recovered within 12 months and beyond to be separately disclosed
- Definition is substantially similar to proposed Schedule VI
- Current and non-current liabilities
  - Liabilities forming part of normal working capital are current liabilities, even if payable after 12 months
  - If the roll over for over 12 months of a liability is expected or at the option of the entity, it is to be reported as non-current liability



# Discussion paper on financial statements

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- FASB and IASB have issued a discussion paper in October 2008 (comments were due by April 2009) on financial statements
- Main highlights are
  - Clear distinction between activities by which an entity creates values, and finances its operations – Business activities and financing activities
  - Business activities to be distinguished between operating, investing activities
    - So, essentially 3 groups emerge
      - operating, investing, financing
  - Continuing and discontinued operations to be shown separately
  - Disaggregation of line items by
    - Function
    - nature

# Model of presentation

Statement of financial position	Statement of comprehensive income	Statement of cash flows
<i>Business</i> <ul style="list-style-type: none"> <li>• Operating assets and liabilities</li> <li>• Investing assets and liabilities</li> </ul>	<i>Business</i> <ul style="list-style-type: none"> <li>• Operating income and expenses</li> <li>• Investment income and expenses</li> </ul>	<i>Business</i> <ul style="list-style-type: none"> <li>• Operating cash flows</li> <li>• Investing cash flows</li> </ul>
<i>Financing</i> <ul style="list-style-type: none"> <li>• Financing assets</li> <li>• Financing liabilities</li> </ul>	<i>Financing</i> <ul style="list-style-type: none"> <li>• Financing asset income</li> <li>• Financing liability expenses</li> </ul>	<i>Financing</i> <ul style="list-style-type: none"> <li>• Financing asset cash flows</li> <li>• Financing liability cash flows</li> </ul>
<i>Income taxes</i>	<i>Income taxes on continuing operations (business and financing)</i>	<i>Income taxes</i>
<i>Discontinued operations</i>	<i>Discontinued operations, net of tax</i>	<i>Discontinued operations</i>
	<i>Other comprehensive income, net of tax</i>	
<i>Equity</i>		<i>Equity</i>