Construction of Financial Statements

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This publication is a complimentary resource provided by IFRS SYSTEM Pty Limited and its related entities and is intended to assist those who have responsibility for, or oversight of, the preparation or production of statutory financial accounts.

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Disclaimer

Introduction

Model or illustrative financial statements are available from many sources. Accounting Institutes and Associations produce them, the upper tiers of accounting firms have them readily available on their websites and there are publishers only too happy to sell their own versions.

IFRS SYSTEM is itself a publisher of illustrative financial statements, producing some 30 sets of Pinnacle Illustrative Financial Statements every six months. 1,500 pages of examples that we have considered marketing as a cure for insomnia, but that's another story.

Whilst model and illustrative financial statements can be very helpful, they are like a map that shows only the destination. They show what the destination looks like, where all the pieces fit and how they should be disclosed, but they do not provide any guidance on how to get to the destination in the first place.

It is that gap this booklet seeks to fill. We aim to provide guidance and direction on the construction of financial statements and we hope to share some of the 'tips and tricks' acquired over many years of financial reporting.

There are some people who believe that all of the challenges of preparing financial statements can be overcome with software. As a developer of statutory financial reporting and accounts production software ourselves we wish this were true. Unfortunately it isn't, even if the software is as good and as powerful as IFRS SYSTEM.

The effective and efficient construction of financial statements requires two things:

- Tools (software) that can do the job, and
- A process that maximises the benefits of the tools

The only thing that we will say here about selecting software is: choose a product that will do what is needed and do so as efficiently as possible. Tools that rely on fixed template structures or work-arounds are more than likely to inflame frustration and inefficiency rather than eliminate it.

After the tools comes the process, and as mentioned earlier, this booklet seeks to provide assistance with developing or reviewing the 'construction' process.

We have tried to keep this booklet 'light' and 'to the point' and we hope all those who read it find it useful.

We also acknowledge that this booklet is written from our point of view, which is just one of many. However after many years, and many thousands of financial statements constructed, we know our process works and we are proud to share it.

If you would like to comment on, add to, or even challenge anything in this booklet, please email us at support@ifrssystem.com.

First things first

Financial statements often take a back seat to the audit; and are prepared after the audit field work is complete, which we regard as counter-intuitive.

The financial statements are - in our opinion - a key piece of audit information. They aggregate data and provide the auditors with the opportunity to see an overarching perspective of the entity's financial performance and position. Accordingly, we consider that a first draft of the financial statements should be prepared prior to the commencement of the audit.

Source documentation

The construction process shown in the following diagram begins with the source documentation. Source documents can be divided into two broad categories i) Trial Balance(s) and ii) Disclosures.

Typically, Disclosures will include, but not limited to, Fixed asset register, Commitments schedule, Minutes and resolutions, Tax returns and workings, Regulatory authority records and Securities exchange information.

The source documents are the construction materials for the financial statements and like all construction there is a direct correlation between the quality of the materials used in the construction and the finished product.

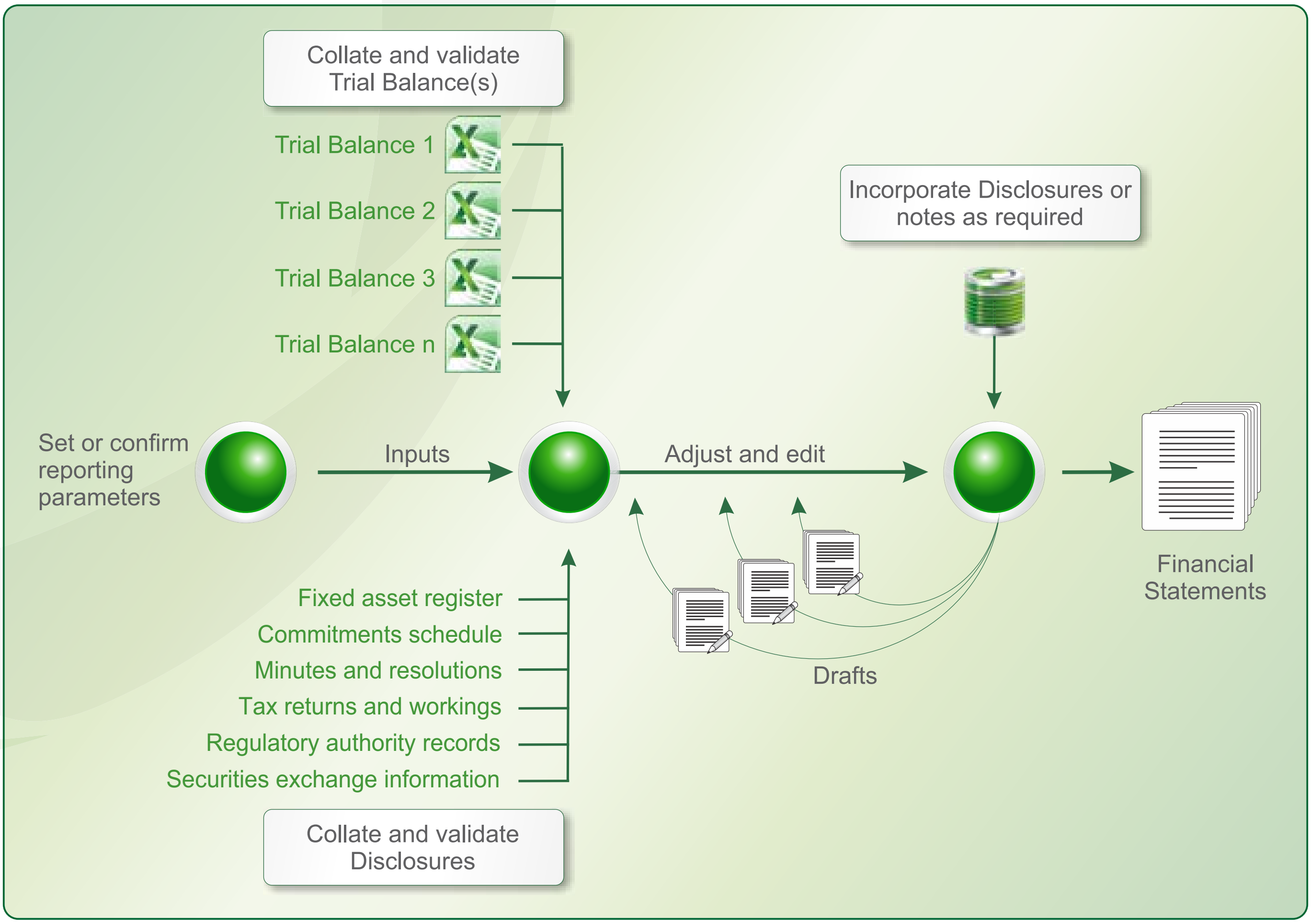
More detailed information on each of the source documents is provided below but as a general rule we suggest gathering the source documents and checking for quality as early as possible.

Often the collection of source documents involves others, so again we recommend communicating any requirements early and clearly.

It is vital that source documents retain their integrity if the auditors are to trust and rely on them. A failure to preserve the integrity of source documents may result in countless wasted hours of unnecessary revision and re-work.

Example: Editing a Trial Balance in a spreadsheet after it has been exported from the General Ledger. This may break the audit trail and cause the integrity of at least three sources (the General Ledger, Exported Trial Balance and Spreadsheet) to be questioned. This will lead to delays and maybe frustration as sources are examined. Once doubts about one document arise it is not uncommon for doubts to be transferred to all documents.

The process depicted in the diagram below is that recommended when using IFRS SYSTEM financial reporting software, however we believe that this or a similar process should be applied regardless of the tool(s) used.



Source documentation continued

Trial Balance(s)

Extract the Trial Balance(s) from the General Ledger(s).

We recommend that Trial Balance(s) be formatted into four columns as follows i) account number, ii) account name, iii) current period and iv) prior period.

Consolidation spreadsheet (if applicable)

Where a consolidation is required, a consolidation spreadsheet will be needed and there are a number of ways to create the consolidation spreadsheet.

For those using financial reporting software, the consolidation spreadsheet can be created by the software. Simply import the Trial Balance(s) extracted from the General Ledger(s) and let the software compile the consolidation spreadsheet. Any eliminations or adjustments that are required should also be made within the software. We recommend this approach as it is generally much quicker, the integrity of the data can be more easily protected and the audit trails (in most cases) are clearer and easier to follow.

An alternative approach is to use a consolidation spreadsheet generated by the entity's Enterprise Resource Planning or Finance system(s). The risk in this approach can be adjustments or eliminations created outside the system as these can, if not managed closely, weaken the audit trail.

The final approach is to create the consolidation spreadsheet manually. The challenge with the manual approach is the inefficiency and risk of error is directly proportionate to the complexity of the consolidation. As such, investments in financial reporting software can sometimes be justified by the benefits of the consolidation features alone.

The approach described above is also relevant for a single entity with only one Trial Balance, as the numbers need to be 'aggregated' for the classifications and sub-classifications within the financial statements.

Disclosures

In order to gather and collate all of the Disclosures we suggest that some time be taken to create a Disclosures file.

The Disclosures file can serve as a resource for identifying which source documents are required, or from whom they will come, and when they are required.

Subject to the way it is created, the Disclosures file may also act as a repository for source information and one from which information can be copied and pasted into the financial statements as required.

For those using financial reporting software, a Disclosures capture tool should form part of the application. Capture tools generally take the form of a file or files that can be sent to others. Once the information has been completed, the capture file is imported thus avoiding the need to 'cut and paste'.

> When considering financial reporting or accounts production software, ask the vendor how their product captures Disclosures.

The following are Disclosure requirements that might be included in a typical capture tool.

Entity historical extract

Obtain a copy of the entity's historical extract from the relevant regulator. The extract will include such things as registration number, entity type, registered and principal addresses, ownership and directors' details. Remember to check that the record is up-to-date.

Fixed Asset Register

This needs to be checked to ensure the cost and accumulated depreciation tie back to the Trial Balance(s) values. The register should also be reviewed to identify assets that should be written off, in particular those with a written down value of zero.

Commitments schedule

The Commitments schedule is most often prepared as a spreadsheet and provides the details of the commitments in the coming financial periods.

The schedule is used to provide information on operating leases, finance leases and capital commitments.

The operating and financial lease information should be summarised by class into the following bands: i) Within one year, ii) One to five years and iii) More than five years.

Capital commitments do not need to be banded.

Source documentation continued

Prior year's tax return(s) and workings

Prior year's tax return(s) and workings are required to perform a 'true-up', which confirms the opening tax balances and any required adjustment.

Minutes and resolutions during the period

A review of the minutes and resolutions will assist in confirming i) any significant changes and ii) details of dividends paid.

Securities Exchange announcements (public entities listed on a Securities Exchange only)

Review all Securities Exchange announcements for the period. This will assist in confirming any significant changes and also ensure that the financial statements are consistent with the announcements.

The Securities Exchange announcements will also include the details of any changes to the holding of any substantial shareholders.

Ready to go - almost

The plan is signed off, materials acquired and checked for quality, a process to ensure the integrity of the construction is in place.

Before donning the hard hat and picking up the hammer and tools, it is time to pause and consider the next set of questions.

Too often we see financial statements that are constructed without too much thought. Generally, the biggest pitfall is simply building on what went before without questioning what has changed.

Taking a little bit of time and asking a few pertinent questions may save much time and result in a more relevant and meaningful set of accounts.

If financial reporting software is being used, many of the following questions are redundant as the software will (or should) address or 'flag' them.

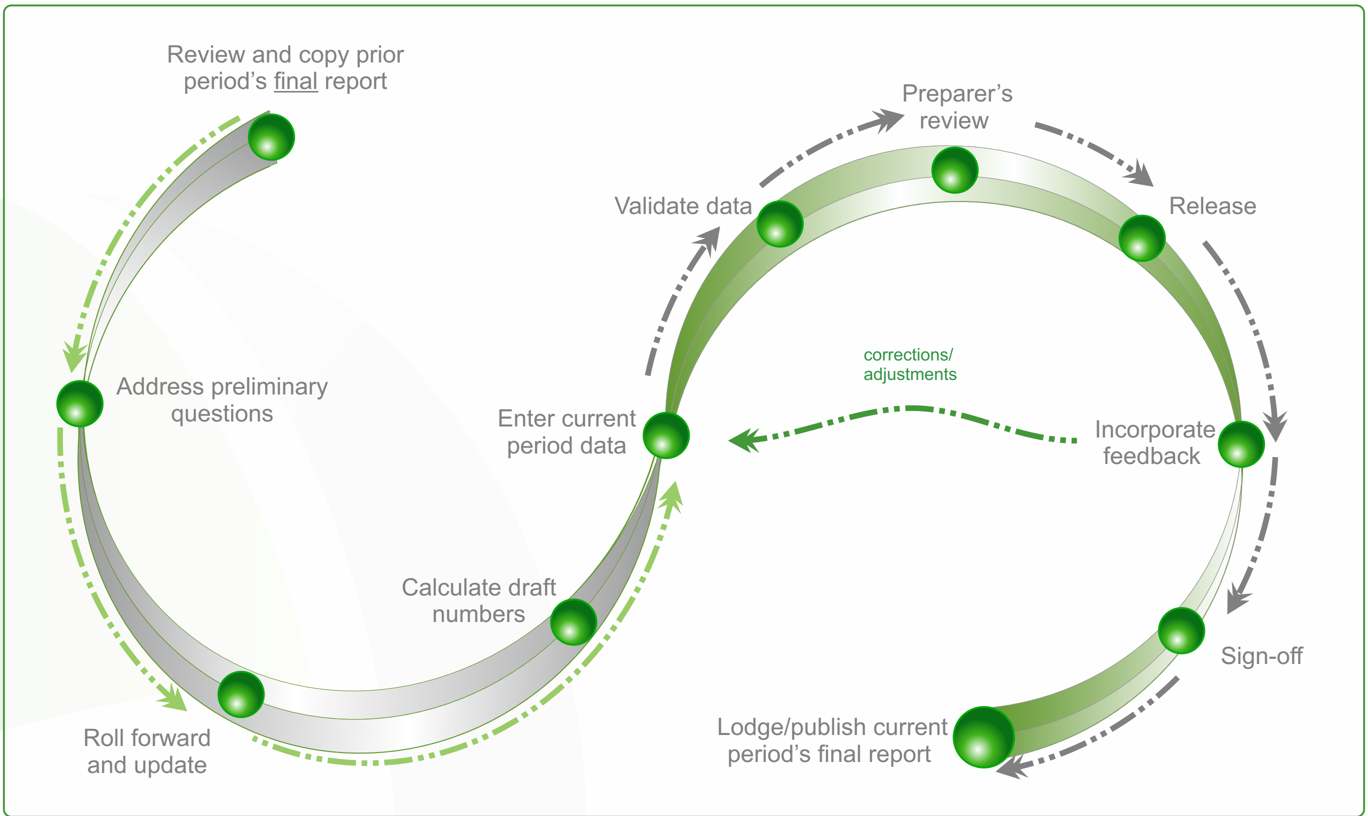
Questions to be considered

If however the construction tools are template based software or 'Word' and 'Excel' consider the following:

- Which reporting framework should be used?
- Is the correct entity type identified?
- If last year's financial statements were prepared under a different reporting framework, how will the change impact the roll forward?
- Have there been any significant changes in the entity's circumstances?
- What are the impacts of any changes to i) Legislation, ii) Regulation or iii) Accounting Standards?
- Are there Disclosures from prior periods that are no longer relevant or required?
- How much (if any) of the financial statements is clutter and could be removed?
- Should notes be re-sorted to present so that they better reflect the key financial measures and focus on areas of most relevance to the entity?
- Is the functional and presentation currency correct?
- Are amounts rounded to the correct level?
- Is the capitalisation, terminology, syntax and grammar correct and consistent throughout?

Bob the Builder (a British cartoon character created by Keith Chapman) applied the mantra 'Reduce, Reuse and Recycle' to his construction projects.

If the mantra underpinning the construction of financial statements is 'Remove, Re-sort and Re-write' that is as good a starting point as any, and let the construction begin.



Constructing the financial statements - step by step

1) Take a copy of the prior period's final report and review it in the context of the answers to any 'Questions to be considered'.

2) If the reporting framework is going to be different to the prior period, make the change now. Don't forget to update the basis of preparation and add, remove or modify Disclosures as required.

3) Make changes, if any, to order or placement of Disclosures and capitalisation, terminology, syntax and grammar. Remember to ensure all new content conforms with any changes made.

4) Roll forward the values and any other general Disclosures that will form part of the current period financial statements. Remember to check headers and footers and update if needed.

5) Enter the current period values (from Trial Balance(s)) and Disclosures.

6) Calculate the first drafts of the:

- statement of comprehensive income and statement of financial position (excluding tax)
- tax disclosures and incorporate them into the statement of comprehensive income and statement of financial position
- Statement of cash flows

7) Where applicable, calculate the first drafts of the:

- business combinations
- financial instruments
- fair value measurement

8) Disclose any significant changes.

9) Check the Disclosures back to the source documents to ensure that they agree.

10) Complete a preparer (self) review including adds-checks, cross-reference checks and overall 'sense' check.

11) Release the financial statements for review.

Steps 5 through 11 are iterative and may be repeated as new or revised information becomes available, however we believe that well constructed financial statements should require no more than four drafts.

The steps above describe a predominantly manual process. If financial reporting software is being used, many of the steps will (or should) be performed automatically.

In the remainder of this booklet, we consider various elements of the financial statements and address some of the more frequent questions and issues that arise during construction or review. This information is not intended to serve as comprehensive guidance on all aspects of the financial statements.

> Many of any of the cross-checks and validations referred to in the following pages should be automated if software is used. Ask the vendor about cross-checks, validations and warnings in their software.

Directors' report

Directors

Use the entity's historical extract (see source documents) to identify directors during the period and their respective appointment or termination dates. Always double check the spelling of the directors' names.

Principal activities

Does the statement on principal activities still correctly reflect what the entity does? Have there been any acquisitions or discontinued operations that should be disclosed?

Review of operations (if applicable)

Always ensure that commentary in the review of operations is newly written.

Significant changes in the state of affairs

A good starting point is the 'matters subsequent to the end of the financial year' in the prior periods report. Such matters are often included here, albeit presented in a different way.

Include any other significant changes that occurred in the period, such as:

- Commencement of operations
- Discontinued operations
- Business combinations
- Purchase or sale of core assets
- Change in financing arrangements
- Breach of financing covenants
- Issue of shares
- Change of entity name
- Change of immediate parent entity
- Change of ultimate parent entity

Matters subsequent to the end of the period

If these matters are disclosed in the directors' report, the wording should be identical to that used in the 'Events after the reporting period' note.

Likely developments and expected results of operations

The report need not disclose any information about likely developments or expected results if, in the opinion of the directors, the Disclosure would be seriously prejudicial to the interests of the entity.

Environmental regulation

Is the entity subject to environmental regulation? If the answer is no, then a statement to the effect of 'The entity is not subject to any significant environmental regulation' would suffice. If the answer is yes, then a more detailed response will be required.

Information on directors

Public entities must disclose information on their directors. Ensure that names, titles and qualifications are correct and that names are spelt correctly. Check if there are special responsibilities e.g. Chair or member of a committee etc. Confirm that meetings of directors agree with any special responsibilities held.

Meetings of directors

Meetings of directors must be disclosed by public entities. Make sure the correct committees are shown and that the number of, and attendance at, meetings are correct.

Company (entity) secretary or secretaries

Public entities must disclose their secretary. Check for changes of secretary within the period.

Directors' report continued

Remuneration report

The remuneration report must form part of the Disclosures of listed public entities.

The principals used to determine the nature and amount of remuneration should be clearly stated, relevant and consistent with the rest of the remuneration report. Matters to be considered would include: executive reward framework, options and other long-term incentives, links between entity performance and individual remuneration and the reaction to the prior period remuneration report.

Details of remuneration

Make sure the remuneration tables for current and prior periods sub-classifications are consistent.

Confirm that the percentages of 'fixed' versus 'at risk' remuneration are correct and that relevant values are correct.

Service agreements

Ensure the service agreements identify the name, title, commencement, term (if not 'ongoing'), base remuneration and scope of the agreement.

If an agreement includes a bonus provision the circumstances under which it would be paid, how it would be calculated and (if discretionary) by whom it will be determined should all be disclosed.

Other matters that might typically be disclosed would be termination provisions, non-solicitation and non-compete clauses.

Share-based compensation

During the period were there any share-based payment arrangements? If yes, these must be disclosed.

Financial report

General

Use the entity's historical extract (see source documents) to check the type of entity and the addresses.

Check the entity's constitution just to 'make sure' the directors have the power to amend and reissue financial reports.

Statement of comprehensive income

Expenses may be disclosed by either 'nature' (raw materials and consumables used, depreciation and amortisation, employee benefits, etc) or 'function' (cost of sales, distribution, marketing, administration, etc).

In recent years there has been an increased incidence of 'hybrid' classification which is i) technically not allowed and ii) problematic as it creates classification challenges and introduces scope for dispute. We recommend that 'hybrid' classifications should be reclassified to 'nature'.

Do expense classifications and fluctuations pass the 'reasonable test' given the type, operations and circumstances of the entity?

What is the level of confidence that revenue and expenses are 'paired' and 'classified' on a consistent basis between the current and prior periods? If there are differences, is there a clear audit trail?

Are other expenses less than 10% of total expenses? (they should be)

Where expenses in the statement of comprehensive income are disclosed by 'function', the depreciation, amortisation, impairment and employee benefits expenses must be disclosed in the notes.

Financial report continued

Statement of financial position

As per the statement of comprehensive income, what is the level of confidence that assets, liabilities and equity are ‘paired’ and ‘classified’ on a consistent basis between the current and prior periods? If there are differences, is there a clear audit trail?

Are there any assets that should be classified as current assets under either 'Non-current assets classified as held for sale' or 'Assets of disposal groups classified as held for sale'? Likewise, are there any related liabilities that should be classified as current liabilities under 'Liabilities directly associated with assets classified as held for sale'?

It may seem obvious, but check that assets are debits and all liabilities are credits. For example, if ‘income tax’ is a debit balance it should be disclosed under assets as ‘income tax refund due’.

Again, check that fluctuations meet the ‘reasonable test’. As a ‘rule of thumb’, any classification that has a variation of +/- 20% should be investigated.

In a consolidation, if the net assets of the parent entity exceed those of the consolidated entity, review the impairment of intercompany receivables or investments in subsidiaries.

Confirm that ‘Net assets’ matches ‘Total equity’.

Statement of changes in equity

Confirm the headers and closing balances in the statement of changes in equity and the statement of financial position agree.

The following items should be disclosed separately:

- Restatement of prior period opening balances (if any)
- Profit/loss after income tax
- Other comprehensive income
- Total comprehensive income
- Contributions of equity (if any)
- Share-based payments (if any)
- Dividends (if any)

Statement of cash flows

In order to prepare the statement of cash flows, the following items would need to be completed:

- Statement of comprehensive income and supporting notes
- Statement of financial position and supporting notes, including relevant reconciliations
- Business combinations note
- Non-cash investing and financing activities note

The following additional information is also required:

- Net income taxes refunded or paid so that income tax movements can be validated
- Proceeds from the sale of property, plant and equipment to validate disposals plus profit less loss
- Proceeds from borrowings in order to gross-up borrowings received and repaid
- Non-cash interest revenue and expense accrued during the year in order to accurately reduce ‘interest received’ and ‘interest paid’ to the cash basis

> ?
>
> Automating the preparation of the statement of cash flows with software can save hours of work. When considering software ask the vendor about ‘cash flows’ features.

Once the statement of cash flows is completed, consider the following:

- Does the net operating inflow or outflow make sense relative to the profit or loss?
- Does the 'Interest and other finance costs paid' exclude any non-cash expenses e.g. intercompany or accrued interest?
- Does the 'Income tax paid' match the movements in the income tax balances?
- Are investing activities correct? Has the purchase or sale of plant and equipment been correctly accounted for (check the PPE reconciliation)?
- Are financing activities correct? Were there any proceeds from issue of shares? Have the borrowings been 'grossed-up' for borrowings received and repaid, rather than a net figure? Was there a dividend paid?
- Are there any material opening foreign currency cash balances that need to be reconverted to the current year rate as 'Effects of exchange rate changes on cash'?
- Confirm the closing cash balances match the cash balances on the face of the statement of financial position (net of any bank overdraft).

Financial report continued

Significant accounting policies

Are the significant accounting policies correct and relevant? Significant accountant polices should be reviewed whenever financial statements are under construction and amended (including culling) wherever appropriate.

When new or amended Accounting Standards and Interpretations are adopted, only list those that are relevant.

The trigger points for a ‘going concern’ are:

- 'current liabilities' exceeding 'current assets' (net current asset deficiency)
- 'total liabilities' exceeding 'total assets' (net asset deficiency)
- cash flow forecasts for future periods
- to a lesser extent a current period loss, especially weighed up next to cash and other current assets

Consider these and whether Disclosure of a 'going concern' is required. If there is a 'going concern', consider the following Disclosures:

- A statement of facts as to why the entity is a going concern
- Separate identifiable liabilities that are unlikely to be called e.g. related party loan
- A letter of support from a controlling entity
- Managements future intentions, which might include capital raising, divesting assets or discontinuing specific operations, etc.

Where the prior or current accounting periods are not full years include an accounting policy.

Ensure the basis of preparation correctly states which Accounting Standards and legislation the financial statements comply with.

Consider the relevance of the wording and if no assets are held at fair value, state 'The financial statements have been prepared under the historical cost convention'.

Trade and other receivables, check the number of days when generally due for settlement and number of days overdue when impairment is considered.

Confirm whether inventories are ‘first in first out’, ‘weighted average’ or ‘specific identification’. Note ‘last in first out’ is not permitted.

Ensure the sub-classes listed in the following accounting policies match those of the relevant note:

- Revenue recognition
- Inventories
- Property, plant and equipment
- Intangibles

Check the number of days when trade and other payables are usually paid.

Only relevant new Accounting Standards and Interpretations not yet adopted should be listed. If management is yet to assess the impact of each, consider a general statement rather than listing specific standards.

Critical accounting judgements, estimates and assumptions

Are the critical accounting judgements, estimates and assumptions relevant? There is little point including 'Provision for impairment of inventories' if there is no inventory. Conversely a 'warranty provision' should be disclosed where it is significant.

Restatement of comparatives

There are three circumstances that can result in a restatement of comparatives and they are i) the correction of an error, ii) a change in accounting policy and iii) a reclassification.

Operating segments (listed public entities only)

When disclosing operating segments the following should be considered:

- Do the operating segments align with the directors' report principal activities?
- Do the operating segments align with the management reports?
- Are there any geographical segments?
- Do financial instruments disclose any receivables risk or concentration with major customers and are the related percentage of sales disclosed?

Financial report continued

Revenue/income

The three classes of revenue/income are i) revenue, ii) share of profits of associates accounted for using the equity method, and iii) other income.

Does the description of revenue/income correspond to both the principal activities and accounting policy? e.g. an entity providing consulting services would likely describe revenue as 'Fees' or 'Services' rather than 'Sale of goods'.

Share of profits of associates accounted for using the equity method. Are there associates or does the statement of financial position show any investment in associates? If yes, ensure that share of profit is correctly classified.

Some of the more common revenue/income items that would be classified as other income might be:

- Insurance recoveries: Did the entity receive an insurance claim payment?
- Net foreign exchange gain: Does the entity transact in foreign currencies?
- Net gain on disposal of assets: Were there any sales of assets?
- Subsidies and grants: Did the entity receive any Government grants or subsidies?

Income tax

Was there a 'true-up' to the prior year's lodged tax return, which confirms the opening tax balances and any required adjustment?

Income tax expense

Confirm the tax effect of the non-deductible permanent difference items such as entertainment, legal fees, impairment of goodwill and share-based payments.

Deferred tax assets and liabilities

Confirm the tax effect of the straightforward items such as: i) provision for impairment of receivables, ii) provision for impairment of inventories, iii) employee benefits, iv) lease make good, and v) warranties etc.

Other items such as: i) prepayments, ii) plant and equipment and iii) accrued expenses should also be confirmed. It may a little harder to confirm these items but confirmation is advisable.

Provision for income tax and income tax refund due

Confirm the balance of either the provision for income tax or the income tax refund due (if operating in multiple jurisdictions there may be both). Does this align with the tax workings and does it pass the reasonable test? e.g. If the refund due exceeds tax paid is it due to an R&D or some other credit?

Discontinued operations

Were there any discontinued operations? This does not have to be an entity - it could be a business or significant product line. Also, it does not have to be a disposal (sale); it could also be a cessation (closure or shutdown).

Trade and other receivables

Is the current and non-current classification correct? Consider any current receivables that have been carried for years without interest or payment - should these be impaired or reclassified to non-current? Are there any receivables that are overdue that should be impaired?

Is there a significant balance in other receivables and if so, what is it?

If applicable, does the banding of the ageing of receivables impaired and not impaired make sense and are the units of measure (days, months, etc.) appropriate?

Inventories

Are inventories stated at the lower of cost and net realisable value? Do the classifications reflect the types of inventory one would expect for the industry the entity is in?

Typically, there are three inventory sub-classifications: i) raw materials, ii) work in progress and iii) finished goods.

Property, plant and equipment

The Trial Balance provides the cost and accumulated depreciation of the various classes of property, plant and equipment; but are these values stated correctly?

Have all of the assets that have a zero written down value or no longer in the entity's possession been written off? A clean and concise Fixed Asset Register (source) will make for a happy auditor.

Is there land and buildings that were revalued more than 5 years (the maximum period) ago?

Financial report continued

Intangibles

Have the intangibles been subjected to impairment testing and are they carried at fair value?

Have the intangibles with finite lives been amortised for the period and does this amortisation match the period quoted in the accounting policy?

Trade and other payables

Is there a significant balance in other payables and if so, what is it?

Borrowings

Is the current and non-current classification correct? Ensure that the principal due in the next 12 months matches the current portion. Are the financing facilities due to expire in the next 12 months? If so, the related borrowings should be current.

Are there any secured liabilities and are the related assets pledged as security disclosed?

Are the financing arrangements correctly disclosed?
Has the finance facility changed or expired?
Were there any breaches of financing covenants?

Provisions

Is the current and non-current classification correct? Consider any current provisions that have been carried for years without change, such as lease make good, and consider reclassifying to non-current.

Likewise, are there any non-current provisions that should be classified as current?

Issued capital

Use the entity's historical extract (see source documents) to confirm the number and classes of shares.

If there is any increase (share issue) or decrease (share buy-back) in issued capital, a reconciliation should be disclosed.

Where applicable, confirm that the capital risk management wording is accurate and reflects the actual practice.

Reserves

Consider the following:

- Revaluation surplus reserve: has the entity revalued assets, such as land and buildings?
- Foreign currency reserve: does the entity have foreign subsidiaries?
- Hedging reserve - cash flow hedges: does the entity have derivative financial instruments assets and liabilities where the movement should be recognised through reserves?
- Share-based payments reserve: does the entity have equity-settled share-based payments?

Retained earnings (retained profits or accumulated losses)

For retained earnings (retained profits or accumulated losses), does the prior closing balance match the current opening balance?

Non-controlling interest (if applicable)

If the subsidiaries note indicates there is a subsidiary with less than 100% ownership, there is a non-controlling interest.

There are three parts to a non-controlling interest: i) Issued capital (what was paid for the shares in the subsidiary), ii) Reserves (the share of the subsidiary reserves, if any) and iii) Retained profits (or Accumulated losses) (the accumulated share of profits or losses, the movement of which should tie into the statement of comprehensive income).

Dividends

Check the entity's minutes and resolutions (source) for any dividends paid. If this is not shown in the report, check if it is incorrectly recorded in expenses? Perhaps the dividends were issued in shares as part of a dividend reinvestment plan?

Financial report continued

Financial instruments (if applicable)

Does the statement of financial position include derivative financial instruments, e.g. forward foreign exchange contracts or interest rate swap contracts, that need to be disclosed in greater detail?

Are there any foreign currency denominated financial assets and financial liabilities (especially foreign subsidiaries)?

Is there any receivables risk or concentration with major customers?

Are the interest rates fixed or floating? Do the interest rates seem reasonable in relation to market rates? Do the interest rates multiplied by the average borrowings for the period tie back in an approximate way to the actual finance cost in the statement of comprehensive income?

Auditor remuneration

In addition to the lead auditor, are there other firms that have undertaken audit work during the financial period and whose fees should be disclosed?

Are there fees for other assurance (such as due diligence) and non-audit services (such as tax), performed by these same audit firms or their related firms, that should be disclosed?

Contingent liabilities

Are there any contingent liabilities? Some of the more common ones might include:

- bank guarantees (which will appear on the bank confirmation letter)
- legal claims (if noted in the directors' report proceedings on behalf of the entity and if not already a provision)
- guarantees of the debts of others (including a single entity that is party to a deed)

Commitments

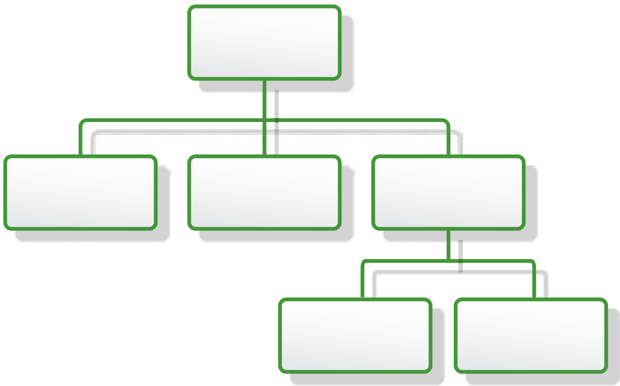
If there were no lease renewals, does the total agree (approximately) to the prior period's total less this year's rental expense (as disclosed in the expenses note)?

For finance leases, do the future finance charges make sense? Does the interest rate (in the financial instruments note, if applicable) multiplied by the average borrowing term remaining approximately tie to the future finance charges?

Are there capital commitments that should be included? e.g. if a new lease was signed close to the reporting date, is there an associated fit-out contract also signed before the end of the reporting period?

Parent entities (if applicable)

Use the entity's historical extract (see source documents) to confirm the immediate parent entity and ultimate parent entity.



Related party transactions (if applicable)

Were there any related party transactions? Sales or revenues will normally result in a receivable, while purchases or expenses will normally result in a payable, as at the reporting date.

As well as intercompany sales, key management personnel related transactions, such as purchases from director-related entities need to be disclosed.

Business combinations (if applicable)

Were any business combinations (businesses or subsidiaries) acquired and do the values of those combinations agree with the statement of financial position? Are these values preliminary or final?

Subsidiaries

Perform a search (via the regulator or even using the entity's corporate website) and confirm the names of the subsidiaries. Have there been any changes of name or deregistrations in the period?

Investments in associates (if applicable)

Are the associates' name, principal activity and percentage interest correct? Does the share of profit match the statement of comprehensive income?

Financial report continued

Events after the reporting period

This note covers the significant events that occurred between the reporting date and signing date.

Has a significant event occurred after the reporting date that affects, or is likely to affect, the consolidated entity's state of affairs in future financial years?

Such events might include, but are not limited to:

- the acquisition of a business combination
- a newly discontinued operation
- the purchase or sale of a core asset
- a change in financing arrangements
- breach of financing covenants

Has a dividend been paid, recommended or declared after the reporting date?

Non-cash investing and financing activities (if applicable)

The cash flow workings will highlight any non-cash investing or financing activities, typically shown as adjustments.

Any increase in lease liabilities, unless related to a business combination, will be 'Acquisition of plant and equipment by means of finance leases'.

Any increase in lease make good provision, unless related to a business combination, will be 'Leasehold improvements - lease make good'.

If there is a business combination and this was partially or wholly financed by a share issue, this is 'Shares issued in relation to business combinations'.

If there is an active dividend reinvestment plan, this is 'Shares issued under dividend reinvestment plan'.

Earnings per share (listed public entities only)

Does the number of shares, on a weighted average basis, correlate to the issued capital note?

Is there any dilution due to options or rights?

Are both the basic and diluted earnings per share quoted on the face of the statement of comprehensive income?

Share-based payments (if applicable)

Were there any options, rights or shares issued as share-based payments (this is usually directors and employees, but may be to others such as suppliers)?

First draft review

Having completed all of the steps, and considered all of the questions, in this booklet it is likely that the 1st DRAFT of the financial statements is now constructed.

No doubt there is still work to be done but if we were to continue the construction analogy, the foundation is laid, the walls are up and the roof is on.

The next key step is to review the financial statements from cover to cover. If reporting software is being used it is also a good time to take a look at any exception or review reports that may be available.

It can be challenging to review one's own work but it is not impossible and it is always better to find (and correct) things before someone else does.

Some things to consider when reviewing:

- Check spelling and grammar. Ensure that the notes and comments are easily understood and portray an accurate picture.

- Is the information in the financial statements consistent with what is known about the entity and does it pass the 'reasonable test'?

- Information in financial statements should be 'objective', 'relevant', 'material' and 'complete', is this the case?

- If reporting software has not been used, or the software doesn't adds check or validate, do the numbers add and tie up correctly?

- Are there detailed audit trails and explanations that can be provided in support of the draft?

The audit process is crucial in ensuring that financial statements fulfil their function of providing a true and fair view of the entity's financial position and performance.

The audit

We believe the keys to an efficient and pain free audit are:

- A structured reporting (construction) process
- A well constructed 1st DRAFT
- Good source documents
- Complete and reliable audit trails