

WORKING CAPITAL & BANK STOCK AUDIT



CEP DISCUSSION BY
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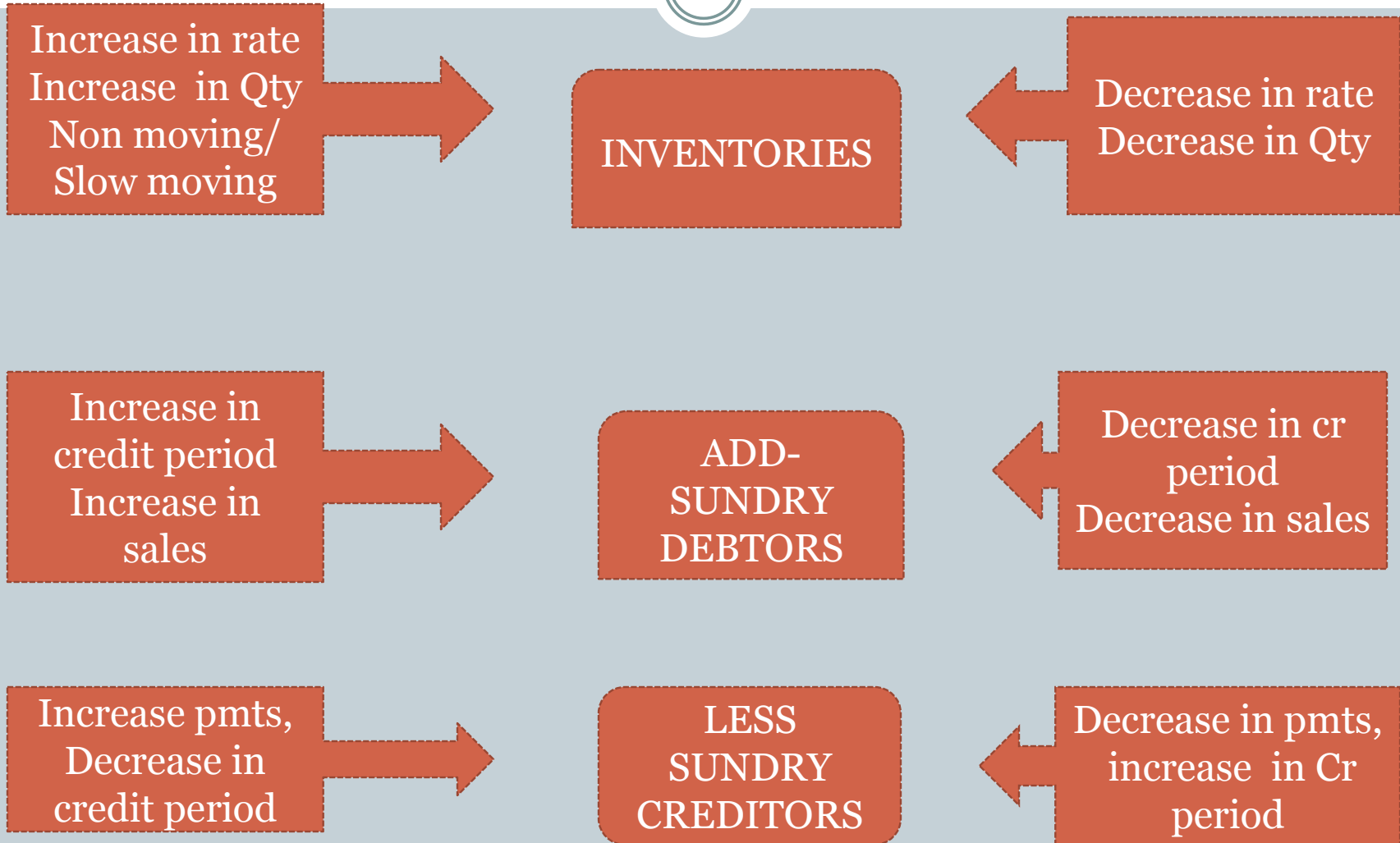
WORKING CAPITAL



WORKING CAPITAL ARE FUNDS REQUIRED FOR SMOOTH DAY TODAY OPERATIONS OF THE UNIT. ON ANY GIVEN DAY IT IS EQUALE TO CURRENT ASSETS LESS CURRENT LIABILITIES= AMT BLOCKED



WORKING CAPITAL



WORKING CAPITAL CYCLE



CASH
BANK
INVENTORIES
& DEBTORS



OTHER INCOME
/ CASH SALES /
RECEIPT FROM
DEBTORS



EXPENSES
PURCHASES
PRODUCTION



CASH SALES
CREDIT SALES



CASH SALES
CREDIT SALES

FACTORS AFFECTING WORKING CAPITAL

- **Uncollected receivables** - If receivables remain outstanding for longer period then chances of default becomes higher
- **Obsolete inventory** - If inventory remains outstanding for longer period of time, then these become obsolete and can't be sold
- **Tight credit** - During poor economic conditions, short term debt becomes less accessible and costly

FACTORS AFFECTING WORKING CAPITAL (continued)

- **Making payments early** - Early payment reduces short term funds available with the company which could have been utilized to meet other working capital requirements
- **Reduced credit limits** - If a company frequently makes late payment to suppliers, then credit limits might get reduced
- **Limits on short term lines of credit** - If banks reduce line of credit to a company, then it will result in liquidity squeeze

FACTORS AFFECTING WORKING CAPITAL

- **Low liquidity positions** - Companies can face low liquidity condition owing to poor financial condition of firm or due to nature of industry in which it operates

WORKING CAPITAL RATIOS



- **CURRENT RATIO = CURRENT ASSETS / CURRENT LIABILITIES**
- **RECEIVABLE TURNOVER = CREDIT SALES / AVERAGE RECEIVABLES**
- **INVENTORY TURNOVER = COST OF GOODS SOLD / AVERAGE INVENTORY**

RECEIVABLE MANAGEMENT



- **Receivable Ageing**
- Tradeoff between credit terms and ability to make sales.
- If credit terms are strict, sales may go down credit terms are too lax then -default on receivables
- Receivables turnover should be comparable to industry standards.

Inventory management



- If inventory turnover is too low, it would imply that too much of capital is tied in inventory and these inventories can become obsolete and never get sold in future
- If inventory turnover is too high, it would imply that firm is maintaining too little inventory on hand and it might result in lost sales due to non-availability of product
- Inventory turnover of a firm should be as per industry standards

Accounts Payable Turnover



- If payables turnover is too low, it would imply that there is excess delay in payments to suppliers. In future suppliers may not agree to such lax payments
- If payables turnover is too high, it would imply that firm is making early payment and this cash could have been used for other working capital purpose or firm could have earned interest on early payment amount

Accounts payable Turnover



- Trade credit (or discount on early payment) may prompt a firm to make early payment (No of days credit, No of days early payment % of discount offered)

BANK STOCK AUDIT



The audit of stock, debtors to workout the amount required for working capital & to safeguard the working capital / funds provided by the bank. To check for diversion of funds & for utilisation for intended purposes

Normally done by retired bank employees, Chartered or Cost accountants- not related with the branch or the unit as concurrent auditor or statutory auditor

Why is BANK STK AUDIT important for CMA?

- **Public Sector Banks (PSBs)** There are a total of 27 PSBs in India [19 Nationalised banks + 6 S B Igroup + 1 IDBI bank + 1 Bhartiya Mahila Bank.] These banks have ,say,70,421 branches
- Private sector banks have say,14,584 branches
- Plus foreign banks have 331 branches. Thus there are 85,336 branches where there is possibility of stock audit assignments.
- Where ever the advances crosses exposure as prescribed by RBI the stock audits have to be carried out by professionals

Continued-----



- It may be possible that fees may not be attractive but if two/ three assignments of say same location are given at one time, then it can be very attractive
- But lot of CMAs all over India can get assignments & through the same, the industry exposure. For new CMAs this can be their introduction to industry

STEPS INVOLVED

- Getting empanelled
- Allotment of assignment of unit for BSA
- Go through the letter carefully & find out special requirements if any
- Get copy of sanction letter (details)
- Whether there is consortium or single bank financing
- Whether pledge or hypothecation

continued



- Check from the party's account the transactions to check the limit enjoyed, overdrawn if any, nature of receipts (direct realisation), use for long term purposes, diversion of funds payment to related parties etc

POINTS TO BE CONSIDERED -INVENTORIES



- **PHYSICAL SAFTY –NATURAL CALAMINITIES**
- **SECURITY OF STOCK**
- **INSURED, IN BANKS NAME, INSURANCE VALUE, VALIDITY**
- **PHYSICAL STOCK – STOCK ARRANGEMENT**
- **COMPARISON - PHYSICAL VIS A VIS BOOK STK**
- **VALUATION METHOD , VALUATION RATE**

INVENTORIES- CONTINUED



- **MOVEMENT- ANY NONMOVING, ABSOLUTE MATERIAL**
- **REQUIREMENT OF PRODUCTION- WHETHER REASONABLE**
- **COMPARING THE CORRECTNESS OF REPORTING, AUTHENCITY OF MIS**

POINTS TO BE CONSIDERED – SUNDRY DEBTORS

- AGING OF DEBTORS – ALLOWABLE AGE
- DEBTORS MOVEMENT / BALANCE REASONABLE
- ACCOUNTING OF SALES, DEBTORS & ITS REALISATION
- WHETHER REALISATION FLOWING DIRECTLY IN THE CC ACCT & PMTS ONLY TO PARTY
- RELATED PARTY SALES TRANSACTION

DP WORKING



- DP WORKED AS FOLLOWS
- INVENTORIES LESS MARGIN =
- DEBTORS LESS MARGIN (90 Days) =
- LESS CREDITORS =
- -----
- D P AVAILABLE =

- W C LIMIT, D P AMT USED VIS A VIS DP CALCULATED AS ABOVE WILL CLARIFY IF EXCESS CREDIT USED

PRACTICAL TIPS



- Check whether banks board displayed
- Study of the industry / unit and other details whatever available like on net or in some records
- Production flow chart
- System of accounting / inventory accounting
- Test check / random check
- Whether cost records are applicable
- From bank records / from party's ledger some unusual transactions

The end



● **THANKS ALL**