

Inside the audit: Part 4 - Trade Payable

Objective:

The objective of trade payables testing is to ensure that all liabilities relating to goods and services received are completely, accurately, and validly recorded, valued, and appropriately presented in the financial statements. This is achieved by performing procedures such as vendor reconciliation, invoice and GRN matching, cut-off testing, review of ageing, and identifying any unrecorded liabilities.

I. COMMON AUDIT PROCEDURES (APPLICABLE TO ALL TRADE PAYABLES)

A. Understanding of Process & Controls

- Understand the purchase-to-pay process, from vendor onboarding to invoice processing.
- Review controls over vendor master creation, changes, and approval workflows.
- Verify controls over three-way matching (Purchase Order, Goods Receipt Note, Invoice).
- Review controls for automated/manual posting of invoices.
- Understand management review over ageing, vendor reconciliations, and overdue balances.
- Check controls over duplicate invoice prevention.
- Review controls over rate/price master to ensure correct rates are applied to invoices.

B. Substantive Procedures – Common Testing Across All Vendors

1) Existence / Occurrence

- Obtain detailed ageing of trade payables and vendor-wise listing.
- Perform vendor reconciliation for major vendors.
- Trace selected payable balances to invoices, purchase orders, and goods receipt notes.
- Send external confirmations to significant vendors, including year-end outstanding balances.
- Match subsequent payments (post balance-sheet date) to validate existence of payables.

2) Completeness

- Review all unmatched GRNs and compare with purchase orders to identify unrecorded liabilities.
- Examine post-year-end invoices to capture expenses relating to the reporting period.
- Review vendor debit/credit notes for timing differences (rate/quantity differences, returns, discounts).
- Evaluate accrued liabilities to ensure all obligations are captured.
- Compare monthly purchase trends to identify missing accruals.

3) Accuracy / Valuation

- Verify invoice calculations, approved purchase terms, and application of rate master.
- Check GST, TDS, and other applicable tax components.
- Review foreign currency vendor balances and recompute revaluation using Reserve Bank of India rates.
- Reconcile vendor ledger balances with confirmations or statements.
- Validate ageing and interest/penalty calculations, including interest on delayed MSME payments.

4) Rights & Obligations

- Confirm legal obligation to pay based on purchase orders, agreements, and delivery evidence.
- Verify that payables belong to the entity and are not personal or related-party transactions.

5) Cut-off

- Match GRNs and purchase invoices around year-end for proper period recognition.
- Examine post-year-end payments to determine if liability pertains to current reporting period.
- For MSME vendors with delayed invoices, ensure accruals are recorded in the correct period even if payment is delayed.

6) Classification & Presentation (Schedule III Review)

- Ensure trade payables are classified under current liabilities.
- Separately disclose:
 - Dues to Micro, Small and Medium Enterprises (MSME)
 - Dues to other creditors
 - Dues to related parties
 - Trade payables ageing schedule (as per Schedule III)
- Ensure unbilled dues are presented as "Trade Payables – Unbilled" or "Accrued Expenses".

C. Analytical Review

- Perform month-on-month and year-on-year payable movement analysis.
- Compare expense-to-payables ratio to identify inconsistencies.
- Review major supplier dependency and sudden changes in payable patterns.

II. SPECIFIC PROCEDURES FOR MSME VENDORS

1) Identification & Verification

- Obtain MSME declarations/registration certificates.
- Verify vendor master status and periodically review updates.
- Check GST and Udyam Registration Number for MSME vendors.

2) Substantive Testing

- Verify outstanding balances with invoices and GRNs.
- Check ageing of MSME payables:
 - Payments beyond 45 days (with agreement) or 30 days (without agreement) → calculate interest.
- Examine delayed payments and pending invoices: ensure accruals are recorded in financials.
- Recompute interest under MSMED Act for late payments and ensure it is recognised as expense.
- Confirm MSME balances via external confirmations.

3) Rate Master / Pricing Verification

- Check that invoiced rates match approved rate master / purchase agreement.
- Investigate differences and ensure proper approvals for rate variations.

4) Financial Statement Disclosure

- Ensure notes include:
 - Principal and interest outstanding to MSMEs
 - Interest paid/payable under MSMED Act
 - Delayed payment amounts
 - Reasons for delay, if available
- Confirm proper classification under Schedule III as "Dues to Micro and Small Enterprises."

III. HIGH-RISK / ADDITIONAL AREAS

- Duplicate vendor codes or duplicate invoices.
- Long-outstanding or disputed payables.
- Advance payments, unbilled GRNs, or pending MSME invoices.
- Foreign currency payables and revaluation.
- Any unusual payment delays affecting expense recognition.