GUIDELINES FOR PREPARING PROJECTED FINANCIAL STATEMENTS

Before entering into the nitty-gritty of the precautions to be taken by the professionals, first of all, I would like to throw some lights on the definitions of the basics of the Projected Financial Statements:

WHAT IS FINANCIAL FORECASTS AND PROJECTIONS?
Financial forecasts and projections are two types of prospective financial statements that attempt to reflect a company’s expected financial position and expected results of operations.

FINANCIAL FORECAST
A financial forecast reflects, to the best of the company’s knowledge, the expected financial results of a future period. It is based on expected conditions and expected courses of action. It is to be noted that in almost all situations, the party responsible for the prospective financial statements is the management of the company.

FINANCIAL PROJECTIONS
A financial projection is different than a forecast in that it is based on hypothetical assumptions. A projection reflects the financial position and results of operations based on a “What if” type of scenario. It is to be noted that only a financial forecast is appropriate for general use.

Now, I would like to touch upon those areas, which needs to be taken care of and needs some fine-tuning before accepting any assignment of preparing/compiling of projected financial statements.

PRECAUTIONS TO BE TAKEN BY THE PROFESSIONALS BEFORE COMPILING PROJECTED FINANCIAL STATEMENTS
1. Make sure that the assumptions used in preparing projected financial statements are reasonable and supported by documentary evidence. Though the compiler (i.e. Professional) is not under obligation to gather the supporting evidences but he should be aware of obvious inappropriate assumptions used to construct the projected financial statements.

2. The compiler of the projected financial statements needs not to be independent but he must disclose lack of independence.
3. Compiler should take a summary of significant assumptions (preferably through Representation Letter from Client) that are used in preparation/compilation of projected financial statements.

4. The professional who has prepared/compiled the projected financial statement should issue a “Compilation Report” for the party who is going to use it.

I personally of the opinion and strongly recommend that professionals should submit the “Compilation Report” along with projected financial statements to make it clear about the extent of checking they have made and the extent of responsibility they are going to take. The format of the report should be more or less in the format as given in Annexure-1.

OTHER MATTERS TO TAKE CARE OF BY THE COMPILER OF THE PROJECTED FINANCIAL STATEMENTS
1. Take an appointment letter from the client, which clearly mention the terms and conditions, time period to complete the job and preferably the fees to be paid.

2. Take a Representation Letter from the management of the co., which usually contain the following matters:
   ~ The purpose of issuing of projected financial statements;
   ~ List of assumptions on the basis of which projected financial statement has been issued and the procedure adopted to collect these assumptions;
   ~ Name of the responsible party (I.e. a financial institute or banker) who is going to use it;
   ~ Report on rating of the company, if any given in the past by any financial institute or rating agency;
   ~ Any attempt made in the past in this matter with any other financial institute or any other professional and result thereof.
PROCEDURES FOR INDEPENDENT EVALUATIONS TO BE MADE BY THE PROFESSIONAL OF THE REPRESENTATIONS MADE BY THE MANAGEMENT

1. Gather the information about the industry, in which client is involved. The information can be gathered from the web browsing or some Govt. / Private publications on the subject matter.

2. Analyse the past financial statements of the client, which include the analysis of relevant ratios, which reflect the financial health of the company.

3. Analyse the past track record of the client regarding repayment obligations.

4. Independent meeting with the concern persons of the management on the subject matter, with specific questionnaire and agenda.

CONCLUSION:
Only after getting Appointment letter, Representation Letter and results of the analysis made, the professionals has to decide about acceptance of the assignment of preparation of prospective financial statements and issuing of any report thereon.