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IMPROVING THE QUALITY OF FINANCIAL STATEMENTS THROUGH TIMELY CLEARING GOOD RECEIPT INVOICE RECEIPT (GRIR)

Aruna S. Abeywickrama¹

¹Chartered Accountant,
Institute of Chartered Accountants of Sri
Lanka
Sri Lanka

**Wewelpanawa Gamage Thushari
Sewwandi²**

²Assistant Lecturer,
Department of Commerce and Financial
Management,
University of Kelaniya,
Kelaniya, Sri Lanka.

ABSTRACT

This paper on “Improving the Quality of Financial Statements through Timely Clearing of Good Receipt Invoice Receipt (GRIR)” reviews a typical GRIR clearing process and attempts to identify the root causes for pending GRIR lines with the objective of improving the timeliness and accuracy of the information provided through the financial statements. The GRIR clearing process of a reputed company operated in Sri Lanka was studied to identify the root causes for pending GRIR lines. When a company raises a purchase order, the supplier delivers the goods and issues an invoice for payment. In the normal course of business, the goods receipts and the quantity invoiced for a purchase order often differ and this ultimately will result in artificial debit or credit balances in the books of accounts. Pending GRIR lines for a longer period of time results in overstated/understated expenses or liabilities and that adversely affects the quality of the information provided through the financial statements. Therefore, it is recommended to clear the GRIR account at regular intervals and especially at the end of every fiscal year in order to preserve the timeliness and accuracy of the financial information. Anyway, when it comes to practice, to reconcile the GRIR account manually and follow up the deviations will become more tedious task. This becomes more difficult for the companies which are handling high volumes of purchases or engaged in purchasing from foreign countries. Clearing GRIR, which is categorized as a non-value adding activity, involves a huge cost and thus to identify the causes for pending GRIR lines will be important. Though the causes may differ from organization to organization, this study identifies the common causes along with their potential impact and the solutions.

KEYWORDS: GRIR (Goods Receipt/Invoice Receipt), Expenses and Liabilities, Financial Statements, Purchase Order, Timeliness and Accuracy, Non-Value adding Activity

1. INTRODUCTION

A Goods Receipt/Invoice Receipt (GRIR) clearing account is a bookkeeping device that is used to update the accounting entries for goods receipts and the invoices to be paid. When a company wants to purchase goods, it raises a Purchase Order (PO) and this acts as a request made to the supplier to deliver the goods. The supplier is committed to deliver the goods in the required quantity and quality as mentioned in the PO and he thereby hands over the invoice for the payment. When the company receives goods, the liabilities will increase in the books of accounts and such liabilities will be settled by entering the invoice and making the payment to the supplier. In the normal course of business, a discrepancy between goods receipts and the quantity invoiced for a PO can always be seen. The GRIR clearing account checks the quantity of goods receipt against the quantity of goods invoiced and then posts a positive or negative balance accordingly in the books of accounts. Pending GRIR lines for a longer period of time indicate that the GRIR clearing process is ineffective and thus actualization of expenses or liabilities is also pending leading to overstated/understated expenses or liabilities. This kind of a situation leads to generate less useful financial information for decision making. Therefore, it is recommended to clear the GRIR account at regular intervals and especially at the end of every fiscal year in order to ensure the presentation of timely and accurate financial information through the financial statements. Anyway, in practice, whenever the companies handle high volume of purchases, to reconcile the GRIR account manually and follow up the deviations will become a tedious task. This will become more complex whenever the company is doing imports because of the different conditions inbuilt in the PO. Depending on the complexity of the process, the companies have created special positions such as GRIR Analysts, GRIR Accountant etc. solely for clearing the GRIR pending entries. As per the indeed.com, the world's number one job site, the annual salary of a GRIR analyst would be around USD 165,000 ("GRIR Analyst Salary," n.d.,). Therefore, GRIR has been one of the top audit findings in most of the companies using SAP as the ERP system. On the other hand, companies focusing on continuous improvement have a tremendous pressure to cut down non-value adding activities such as GRIR clearing. Therefore, simplifying this process as much as possible is of vital importance in today's business world.

Accrual Accounting and GRIR:-

The objective of general purpose financial reporting is to provide financial information about the

reporting entity that will be useful for existing and potential investors, lenders and other creditors in making their decisions about whether to provide resources to the entity. Those decisions involve buying, selling or holding equity and debt instruments, and providing or settling loans and other forms of credit (The Conceptual Framework for Financial Reporting, 2012). Accrual accounting is a technology for improving financial reporting and disclosure (Ball & Shivakumar, 2006). On the other hand, Sri Lanka Accounting Standard – LKAS 1 states that “an entity shall prepare its financial statements, except for cash flow information, using the accrual basis of accounting”. Therefore, all the accounting software, especially the ERP systems, are designed such that they support the accrual accounting concept. Hence, once the goods are received to the company warehouse, a GRN is raised in the system and accruals are passed automatically to recognize the expense and the liability. GRIR is one step ahead of this concept where it recognizes the landed cost of the item, thus all the related costs are getting accrued at the time of receiving the goods. The liability should be recognized at the total landed cost and should not be limited to the selling price of the material. Therefore, all the costs such as duty, freight, handling charges and insurance should be accrued in the accounts. A liability should be recognized in the balance sheet when it is probable that an outflow of resources embodying economic benefits will result from the settlement of a present obligation and the amount at which the settlement will take place can be measured reliably. In such circumstances, recognition of liabilities entails recognition of related assets or expenses. (The Conceptual Framework for Financial Reporting, 2012). As per the GRIR concept, the total liability is recognized at the rate mentioned in the purchase order. Anyway, the costs of support services attached to the purchase order (excluding the main supplies and the duty payments) such as the freight charges and handling costs, are based on estimated figures. This is the reason for why a company might have created unnecessary accruals which hinders the profitability for a given period. Although these accruals are getting actualized over time, the periodic results will be inaccurate due to the delay in clearing the GRIR difference.

An organization is required to maintain a healthy GRIR outstanding. In other words, there should be a clear process to identify and clear GRIR lines before they become overdue. There is no such definition to categorize the overdue GRIR lines and it depends on the company to company due to the average credit period of the vendors' and average time period for a goods receipt to get cleared from the system. The case studies done up to now have

referred to this process as a one which is clearly linked with the process improvements and decrease the cycle time of GRIR.

2. METHODOLOGY

The aim of this paper is to review a typical GRIR clearing process and to identify the root causes for pending GRIR lines. The GRIR clearing process of a reputed company operated in Sri Lanka was studied for this purpose. The GRIR clearing process is illustrated and reviewed through a hypothetical example constructed by taking the actual clearing process of the company into consideration. Current situation analysis, Cause and effect analysis, five-why analysis, brainstorming, cost-benefit analysis and effort-benefit analysis were the main techniques used for the study.

The current situation analysis done in the actual context revealed the problem of Pending GRIR lines. A contributor analysis coupled with Pareto analysis were used in this regard. Contributor analysis starts with breaking down the overall results in to small divisible components. This becomes easier with a process flow diagram drawn to depict the entire end-to-end activities of the process. The findings from contributor analysis were helpful to quantify the impact that each of the components do have on the overall result of the company. The results of contributor analysis were used for Pareto analysis, which is a statistical technique that can be used to select a limited number of tasks that may produce a significant overall effect on the problem. Having identified the problem, pending GRIR lines, the possible causes were identified through the cause and effect analysis. The root causes were identified through five-why analysis and brainstorming. Having identified the root causes of the problem of pending GRIR lines, the solutions for each root cause were generated. These solutions were further analyzed through the cost-benefit and effort-benefit analysis in order to identify cost-effective solutions. The implementation plan clearly specifies the deadline along with the responsible person. One of the most important stage of the GRIR process is to sustain the results for future period. Employee engagement and training are treated as critical in this regard. The following techniques can be used to sustain the results for the future.

- **Creation of a Standard Operating Procedure (SOP):-**

Standard Operating Procedure for total GRIR process includes the activities, roles and responsibilities of each user. Clear cut responsibilities should be specified for each user with the timelines and frequency of actions. It is required to identify the revision date for the SOP to be updated with the changes of the business processes.

- **Establishing an Error Log:-**

Stakeholders can repeat the same error many times and this can be avoided by taking long term solutions. This is possible to be done by maintaining a learning log which includes all the details of the errors done and the solution taken. This error log can be shared with the stakeholders in regular intervals.

- **Conduct Vendor Reconciliations:-**

The company can periodically request for outstanding statements from the vendors so that those can be reconciled with the payment system in order to identify any discrepancies. For example, if there are invoices outstanding in the vendor statement for a longer period of time, the reconciling person can do a search through the purchase order number linked to that payment. If there are issues regarding the GR or invoice, those issues can be resolved on timely basis.

- **Objective Cascading and Establishing the Review Mechanism:-**

Sustaining the results is possible by establishing an objective for GRIR and monitoring the same in regular intervals. The information generated through the contributor analysis and Pareto analysis can be helpful in identifying proper objectives and Key Performance Indicators (KPIs) for the GRIR process. Once the main objective is identified, the same can be cascaded down in to smaller objectives for each stakeholder in the process. The performance of those objectives should be measured using KPIs in regular intervals. It is crucial to identify a review mechanism to discuss the matters relating to the GRIR process

3. RESULTS

3.1 Review of GRIR Clearing Process:

A Hypothetical Scenario:-

Assume that a company has raised a Purchase Order (PO) to purchase 1,000 kgs of sugar to be used in the production process at the rate of USD 10/- from the supplier X. As per the PO, the supplier should deliver the consignment to the company warehouse. No accounting entry is passed at the time of raising the PO. Once the supplier delivers the goods to the warehouse, the warehouse officer will check the quantity and raise a GR against the above PO. If the supplier has supplied 1,000 Kgs of sugar without any excess or shortage, the warehouse officer will feed exactly 1,000 kgs in to the system. It is at this point that the supplier will transfer the risk and rewards to the company and thus the accounting entries shown by the Table 3.1 will be initiated in the system. This transaction will result in increase of both inventories and payables causing both assets and liabilities to increase by the same amount. Once the supplier sends the invoice claiming

the amount to be payable for the goods supplied, the company needs to enter the invoice against the same PO. Once the invoice is entered in to the system, it will be triggered for payment considering the pre-established credit terms with the supplier. If the supplier has correctly raised the invoice for a value of USD 10,000, in the event that the supplier is not registered for Value Added Taxes, the accounting entries will be as shown by the table 3.2. Those entries result in simultaneous increase and decrease of the payables by the same amount creating no impact on the balance sheet liabilities. This happens because both GRIR account and supplier payable accounts are categorized as payables. If the transaction occurs in this manner, the GRIR account will get cleared properly as shown through the Table 3.3. But when there is a mismatch between GR and IR, both entries will hang in the GRIR account without being automatically cleared. Since the real case transactions are not as simple as explained in the above example, it is unavoidable to create such pending GRIR lines.

3.2. Causes for Pending GRIR Lines:-

Table 3.4 exhibits the common reasons for pending GRIR lines. Those common causes include;

- Goods received physically but not the invoice received
- Invoice received but not the goods received physically
- Invoice and goods received but the system entry is pending
- Quantity mismatch in GR vs. IR
- Payment conditions created in the Purchase order without actual payable balances

The first two causes have no financial impact whereas the next three causes will result in understate/overstate of assets, liabilities and expenses as shown through the table. The solutions provided for each of the above five causes will be as follows.

- Effective procedure to collect the invoice at regular intervals and feed in to the system
- Accepting the invoice only upon the delivery of goods
- The best practice of raising GR once goods received
- To improve the discipline of goods receipt and invoice entry
- To improve PO creation process

4. SUGGESTIONS

Even though the impact of pending GRIR lines on the financial statements is immaterial (as the pending lines consist of debits from IR and credits from GR), it is the best practice to minimize the long outstanding GRIR lines. Therefore, GRIR reconciliation is treated as one of the main finance health checks. Accuracy of the GRIR reconciliation is measured based on the long outstanding GRIR lines which are not cleared. In order to maintain a healthy GRIR outstanding, the vital part is to reconcile the outstanding lines regularly and follow-up with the stakeholder for specific actions. In order to do this, it is vital to maintain high standard of employee engagement level as this is purely a manual process. On the other hand, employee engagement is vital to provide long lasting solutions for the repetitive errors and sustain the results for the future.

5. CONCLUSION

This study was done with the objective of reviewing GRIR clearing process to identify the reasons for pending GRIR lines. The study revealed that neither a manual nor an automated process would be effective for clearing GRIR lines due to the drawbacks inherent in each of them. Even though pending GRIR lines have a minimal impact on the financial statements, pending for a longer period of time has to be avoided to ensure the quality of financial information provided for decision making. Clearing GRIR is a non-value adding activity for an organization which involves a huge cost and hence clearing GRIR account at regular intervals is recommended. The causes identified for pending GRIR include;

6. FIGURES, TABLES AND REFERENCES

6.1. TABLES

Table 3.1: Accounting Entries at the time of Goods Receipt

GL Account	Entry	Amount USD	Calculation
Sugar Inventory Account	Debit	10,000	1,000 Kg X 10.00 per kg
GRIR Account	Credit	10,000	

Source: Author

Table 3.2: Accounting Entries at the time of Entering the Invoice

GL Account	Entry	Amount USD	Calculation
GRIR Account	Debit	10,000	1,000 Kg X 10.00 per kg
Supplier X	Credit	10,000	

Source: Author

Table 3.3: Accounting Entries in GRIR Account

GL Account	Entry	Amount USD	Remarks
GRIR Account	Debit	10,000	At the time of Goods Receipt - GR
GRIR Account	Credit	10,000	At the time of Invoice Receipt - IR

Source: Author

Table 3.4: Common Reasons for Pending GRIR Lines

Reason for un-cleared GRIR	Impact	Action to be taken
Goods received physically but not the invoice received in the books of accounts.	No financial impact, but not in line with financial/operational best practices.	Effective procedure to collect the invoice at regular intervals and feed in to the system.
Invoice received but not the goods received physically	No financial impact, but not in line with financial/operational best practices.	Wait till the goods received. To accept the invoice only upon the delivery of goods must be practiced.
Invoice and goods received but pending system entry	Understate the assets / expenses	The best practice of raising GR once goods received
Quantity mismatch in GR vs IR.	Understate / overstate assets / expenses / liabilities depending on the situation.	To improve the discipline of goods receipt and invoice entry.
Payment conditions created in the PO without actual payable balances.	Overstate the assets / expenses.	Need to improve the discipline in PO creation process.

Source: Author

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